There are no translations available.

Preliminary remarks

Arbitrability of the disputes over order papers is not quite clear in the central Europe. Despite some cases of mandatory arbitration, arbitration agreement is seen as substantial prerequisite of jurisdiction of arbitral tribunal.

In germanic continental[1] judicial practice and also in jurisprudence has been prevailing approach (until recent landmark decisions, that issues, involving erga omnes effects or/and substantial change of the legal position of non-parties are non-arbitrable

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It is widely known that non-arbitrability concept was built on the limits of arbitrability laid down by quite ambiguous wording of respective statutory laws. Respective laws contained reference, that subject matter of dispute is arbitrable if such subject matter could be subject to (court or out-of-court) settlement.

Effects on the non-party, statutory registers and “erga omnes" and also disputes where remedy sought were declaratory judgement, were long classical reason to deny possibility of settlement (compromise) and thus also arbitrability of the respective cases.

Non-arbitrability has been long one of reasons for setting aside number of arbitral awards in Czech Republic, Slovakia or Russia, concerned with „erga omnes“ entitlements, such are (land) property disputes.[3] Other way around, swiss PILA (Art. 177) provides that any dispute involving property can be the subject matter of an arbitration.

Meanwhile, recent landmark decisions of Supreme Courts both in Slovakia and in Czech Republic have changed “map of battlefield” and now it is quite clear that arbitration agreement can include in its scope also declaratory rulings, if there is some kind of commercial or property link.

Main reason for arbitrability of such disputes is focused to impossibility of cutting the judgement as to validity of contract or its part as preliminary question from arbitration. Therefore in any arbitration where remedy sought is pecuniary (in principle payment of debt or damages) arbitrator has undisputed jurisdiction to assess the contract between parties or its part as null and void, and also, in specific cases the validity and scope of application of some terms between third parties and participants of arbitration.

Bearing in mind pecularities of order papers issuance and lifecycle, and the prospect of multiparty arbitration arising from such instruments, there is interesting novum in the CEE law of corporations.

In the newly enacted (2013) **Business Corporations Act (Czech BCA)** conditions for new order papers „kmenové listy na podíly“ (shares certificates) which emitent may be limited liability company, issuing such order papers to its shareholder therefore effecting change of shareholders via changing of holder of the certificate.

In such an environment, some new questions would be raised concerning scope of arbitrability and prerequisites as to arbitration agreement in such a cases. This papers is intended to show some of opportunities based on new enactments with cautious regard to jurisprudence and case law in most concerned jurisdictions.

Main open questions are:

1/ Would be arbitration agreement concerning the order papers declared null and void citing non-arbitrability, or the subjective scope of arbitration agreement, and in what circumstances ?

2/ Can the arbitration clause in the main contract bound parties of order papers issued on the basis of such contract ?

3/ Can the arbitration clause in the Articles of Association or Shareholders Agreements bound the members acceding such instrument by virtue of the order paper ?

Tour de horizon:

Arbitrability of the Disputes on Promisory Notes from Singapore via “German expert” in Honkong to the Prague

Interestingly enough I will start with reference to case not from civil law country.

The Singapore High Court held that "*a bill of exchange is a separate contract from the contract pursuant to which the said bill of exchange was furnished* "
(see paragraph [25]) citing the Singapore Court of Appeal decision of
Wong Fook Heng v. Amixco Asia Pte Ltd
[1992] 1 SLR(R) 654).
[4]

The High Court then considered the English House of Lords case of *Nova (Jersey) Knit Ltd v. Kammgarn Spinnerei GmbH*
,
[1977] 1 WLR 713 where the law lords held (by a majority) that a stay of the English court action should be refused because the appellant's claim on the bills of exchange did
not fall within the arbitration clause in the partnership agreement between the parties
. Those bills of exchange constituted separate and independent contracts (see paragraph [31]). The arbitration clause read,

“18. Arbitration agreement

“All disputes arising from the partnership relationship or occasioned by (or ‘in connection with’) the partnership relationship between the partnership and the partners shall be decided by the arbitration tribunal provided for in a separate document.”

The *Nova* case was followed by the Hong Kong Court of Appeal in *Pacific Forex Ltd v. Lei Kuan Leong* [1999] HKCA 364
where the court held at paragraph [11] that,

“The approach to be adopted in Hong Kong law is no different from that in English law … A bill of exchange is not valid if it incorporates an arbitration clause. To hold that an arbitration clause referring to disputes arising from the underlying agreement, applies to bills of exchange would make “a very substantial inroad upon the commercial principle on which bills of exchange have always rested.” Accordingly there must be a plain manifestation in the arbitration clause that it is to apply to bills of exchange if the presumption against taking bills of exchange into arbitration is to be rebutted. As Lord Russell indicated, there is an inconsistency between the nature and function of such a bill and an arbitration clause.”

However, the Singapore High Court declined to follow *Nova* (and the cases following it), first confirming “stay for arbitration” (that means stay of proceeding before court to facilitate arbitration according arbitration clause but not prejudicing the final answer to question of

arbitrability).

Shaun Lee also remind us about *Pacific Forex* case, where Hong Kong Court of Appeal cited "german expert" about german approach:

"In the case of bills given by merchants in payment of the price of goods it cannot, if there is any doubt, be assumed that a clause providing for submission of disputes to arbitration applies to claims under the bills.(…)A very plain manifestation of intention to extend an arbitration clause to claims under bills of exchange is needed to rebut the presumption that businessmen neither wish nor expect bills of exchange to be taken into arbitration."

As Shaun Lee concludes quoting the recent judgements, Singapore Courts moved away from "presumption against taking bills of exchange into arbitration", instead forming new approach of presumption for arbitration, or better "presumption to single forum", reasoning, that if parties did not explicitly agreed otherwise, arbitration agreement for underlying contract shall be construed as covering also bills of exchange.

Now we can turn back to Europe, to the very field of the german law influence - to the Czech case law.

In the case *No. 5 Cmo 342/2007* High Court of the Prague basically followed the HKCA cited "german expert" doctrine, reasoning:

" If an arbitration agreement relating to a claim secured by bill of exchange/promissory note *doe s not clearly stipulate that it also covers claims from the bills of exchange,*
then the claims from promissory note/bill of exchange are not subject to arbitration, and must be presented for resolution to a court."
[5]

Similarly Supreme Court of Czech Republic held in case No. 29 Cdo 1130/2011 of May 31st 2011, that claims arising from bills of exchange/promissory notes are arbitrable.

"(1) (a) Claims arising from bills of exchange/promissory notes are property claims if an obligation to pay a particular sum of money is incorporated in the bill of exchange/promissory note, therefore a dispute over the payment of a bill of exchange is a property dispute as provided for in the Section 2(1) of the Czech Arbitration Act.

(2) (a) Nature of the matter commonly allows settlement in matters in which the parties are involved in typical bilateral relationship, providing substantive law does not prohibit the parties from regulating their legal relationships by dispositive acts. Consequently, the nature of the

matter excludes the possibility of settlement particularly: in proceeding which could be commenced by court without motion of party, in matters in which the courts decides on party's personal status and in matters in which substantive law does not allow settlement by agreement of the parties to the legal relationship."[6]

This ruling is of twofold eminence. First is mention about promissory note as property claim with prerequisite of "obligation to pay sum of money" to be incorporated in promissory note. In fact, Supreme Court consequently opined, that blank promissory note is also obligation to pay sum of money (though not indicated in the bill of exchange/promissory note as of issuance).

Second is description of the matters which commonly allows settlement. As we can see, order papers are not 'typically bilateral' other way around, it is instrument evolved for trading, and therefore for moving step by step among broad 'critical mass' of endorsees/endorsers, and via SC ruling involving in the effects of arbitration agreement e.g. guarantors.

German expert again

Surprisingly enough (in the light of german expert cited by HKCA), in german jurisprudence and also arbitrability of bills of exchange/promissory notes (Wechsel) is practically unopposed.

For example Rolf A. Schütze[7] is pointing out not the problematic arbitrability with respect to the separability of the arbitration agreements, its scope or non-signatories, but instead the very fact of quick promissory notes documentary proceeding (consisting of initial proceeding without knowledge of the debtor, and 'nachverfahren' which is first access for defendant to the court) before civil courts and thus reasonability of arbitration in such cases, where parties choosing arbitration waive effective measures of the "Urkundenprozess".

Turning eyes from literature *(I admit that it would be questionable if one piece of Rolf A. Schütze great works is enough, but for the purpose of this paper I answered positive)* to case law, we will find, that in Germany there is no problem with arbitrability, or separability of the arbitration agreement.

In *III ZR 214/05* Bundesgerichtshof (BGH) rendered decision which only confirmed that parties which agreed on arbitration in dispute concerning promissory note waived also access to "Urkundenprozess". In similar terms also OLG Celle ruled in Case No. *5 U 86/05* dismissing the appeal against termination of proceeding before state courts due to the arbitration agreement including promissory note.[8]

Also in the case No 18 U 83/00 the OLG Köln annulled decision of the first instance court which was issued in the documentary proceeding on promissory notes (wechselprozess, urkundenprozess) in the exact case where broad arbitration agreement was signed, and defendant particularly challenged jurisdiction of german courts of law.

Arbitration agreement was stipulated in Partnership Agreement (Gesellschaftsvertrag) , and reads as follows:

“For all disputes arising out of the Partnership agreements, whether of shareholders among themselves in matters of the company or questions of the legal validity of the Partnership agreement and of this arbitration agreement, the ordinary courts of law be excluded and - if legally permissible -instead the decision shall be made by a court of arbitration. This also applies for clarification of points of doubt and the elimination of inequities and hardships. “

As OLG stated in reasons: with words "disputes arising from these Partnership Agreements"are not only meant those that relate specifically to one of the articles of association, but, mutatis mutandis, all company-related disputes. The Partnership Agreement established by its conclusion and content position of the Company and at the same time determined the rights and obligations of the shareholders to the Company. The present dispute relates to the relationship of the defendant as a shareholder against the applicant.”[9]

Back to Prague: Shareholder and agreement in writing

In the case of the *31 Cdo 1387/2010* Supreme Court remanded case to lower instances with dangerous application of precedence of european human rights law.

“ Even though the applicability of an arbitration clause also to shareholders who did not sign the acquisition agreement was confirmed on several occasions by the Supreme Court, as well as by the Constitutional Court, the Supreme Court decided, in this case, to change the established case law and it ruled that the clause is not binding on shareholders who did not sign the agreement.

The Supreme Court did so in the light of the Judgment of the European Court of Human Rights in Suda vs. Czech Republic (Application no. 1643/2006), which considered such an arbitration clause to be violating the right to a fair trial under Article 6 of the Convention for the Protection of Human Rights and Fundamental Freedoms. Since the application of the Convention takes precedence over the application of Acts, it was not possible to apply Section 220k of the Commercial Code based on which such arbitration clauses had been previously allowed.[10]

This ruling is of paramount eminence to the founders of limited liability company, causing concerns as to drafting Partnership Agreements and also Shareholder Agreements and Certificates.

Conclusions and Take-Aways

Summarizing above mentioned changes in court practice we can assume some conclusions, not necessary amounting to answers on the aforementioned questions.

1/ Would be arbitration agreement concerning the order papers declared null and void citing non-arbitrability, or the subjective scope of arbitration agreement, and in what circumstances ?

In the present circumstances, declaration of arbitration agreement as null and void on the grounds of non-arbitrability is improbable. Instead the subjective scope of agreement will be more sensible to challenges.

Good and simple way is to include the arbitration agreement in short terms or at least reference to it directly in the promissory note, and also Shareholder Certificate.

As best practice cautious draft of arbitration clauses in Partnership Agreement and also in Shareholders Agreement and Shareholder Certificates which company will issue is recommended.

2/ Can the arbitration clause in the main contract bound parties of order papers issued on the basis of such contract ?

In principle, as is proven by aforementioned case law, in continental law prevails broad definition of scope of arbitration agreements, but most recent development influenced by ECHR could evolve to situation of widespread denial of binding nature of the main contract, or underlying contract as to parties of order papers, particularly in cases of change in persons to be bound by arbitration agreement, which was not signed by them.

3/ Can the arbitration clause in the Articles of Association or Shareholders Agreements bound the members acceding such instrument by virtue of the order paper ?

At first sight there is similarity with question No. 2) but bearing in mind that order papers will be transferred by virtue of signature at the paper, if cautiously drafted, this clauses will be valid and binding to those shareholder.

As matter of clarity, there are diferences between arbitration agreement and its subjective scope in the case of its integration in Articles of Association and Partnership/Shareholder Agreements on the one side, and in the Shareholder certificate on the other side.

By virtue of taking certificate and signing as shareholder, new shareholder is always successor of the original one, what shall be construed as succeeding to Articles of Association and P/SA (MoA), therefore in the main constitutive document of the Company founders will include arbitration clause also shareholder certificate issued without arbitration clause would be treated as instrument of accession to arbitration agreement.

With regard to ECHR pratice and SC 31 Cdo 1387/2010 would be preferable to include arbitration agreement also in the Shareholder Certificates.

Notes

1) Under term **germanic continental** shall be included jurisdictional and jurisprudential tradition of german speaking states, some of successors of Austria-Hungary (Czech Republic, Slovakia, Hungary, Croatia, Slovenia) and at least in some degree also former constituents of Soviet Union.

2) Objective arbitrability determines the subject matters which can be referred to arbitration. An award may be set aside due to non-arbitrability of the subject-matter of the dispute.

3) Arbitrability of real estate property disputes was broadly discussed in Russia, and undervent major case law change with regard to the landmark decision of Constitutional Court, opening door for (though limited) arbitrability of the disputes over immovable property , but this question is not discussed in the present paper. Also in Czech Republic there is landmark decision of High Court Ostrava concerning real estate arbitration. Both cases provides for distinguishing between "obligationrecht" and "sachenrecht".

4) For in-depth analysis of recent development in Singapore: Shaun Lee, Can a Claim on dishonored check(s) avoid a stay for arbitration ? http://singaporeinternationalarbitration.com/2013/07/18/can-a-claim-on-dishonoured-cheques-avoid-a-stay-for-arbitration/ last access: 15.8. 2014, and Shaun Lee, Case update: (1) Governing law of arbitration determines scope of arbitrability,(2) Disputes on Bills of Exchange falls within the scope of arbitration clause: http://singaporeinternationalarbitration.com/2013/12/26/yafriro-hc/

5) According to prof. Bělohlávek in: Arbitration Law in Czech Republic, decision was quite suprising for it does not require arbitration agreement to be concluded exclusively concerning claims from bills of exchanges, only requiring "clear understanding of parties" over the scope of arbitration clause.

6) Judgement (czech text only) available at www.nsud.cz in search engine of the court (despite the fact of english version of the website there is not full database of judgements in english).

7) Zum Urkundsschiedsvervahren, In: Lebendiges Recht

8) For german case law search engine at www.jusmeum.de was uses with latest access 30/09/2014

9) Number of the similar cases were brought to the german courts as for example OLK Koln No 19 Sch 30/12 confirming jurisdiction and validity of the arbitration agreement.

10) Resumé accessible at http://www.nsoud.cz/JudikaturaNS_new/ns_web.nsf/web/DecisionMaking~Decisions~2012_3_14___31_Cdo_1387_2010__resume_~?openDocument&lng=EN, last access: 5/10/2014