Arbitration agreements in insolvency proceedings

Madrid, November 2014

A recent decision by the commercial court of Madrid number 6 dated September 2, 2014 has ruled on the effects of the declaration of insolvency on arbitration agreements.

Grupo Empresarial Acerta, S.A. (GEA) and Inter Ikea Centre España, S.L. (IKEA) entered into a project management agreement relating to the construction of a shopping center in 2007 (the "main agreement"). The main agreement included an arbitration clause.

GEA was declared insolvent in 2010 and asked the court to terminate the main agreement alleging that was in the insolvency estate's best interest. After a pre-trial hearing, the parties reached a partial settlement agreement terminating the main agreement that was approved by the court. However, the court's approval did not considered the economic consequences of such termination.

A year and a half following the partial settlement, GEA brought an action against IKEA. IKEA alleged, amongst other issues, lack of jurisdiction based on the arbitration clause.

The commercial court of Madrid dismissed the lack of jurisdiction and found itself competent to hear the claim.

In its reasoning the court analyzed the treatment given by the Spanish Insolvency Act (SIA) to arbitration clauses, both before and after its 2011 reform. The general rule is that courts dealing with the insolvency proceedings are also competent to resolve disputes which affect the insolvency estate. As a result, the SIA provided for an automatic suspension of the effects of arbitration agreements during insolvency proceedings. However, the 2011 reform changed this rule, providing that arbitration agreements remain effective, unless the judge considers that they can be detrimental to the development of the insolvency process. To take such decision the court should take into consideration, according to this judgment, the circumstances of the insolvency proceedings in order to ensure an organized, quick and coordinated process.

As the judge explained in his ruling, suspension of arbitration agreements has the effect of releasing the parties from their obligation to submit their disputes to arbitration. This is so regardless of whether the party to the arbitration agreement that is declared insolvent is the plaintiff or the defendant.

Turning on the particularities of the case, it is clear that GEA's insolvency was declared in 2010 and so the arbitration clause was subject to the old SIA regime. Therefore, the automatic suspension of arbitration agreements was not subject to the discretion of the judge.

But the judge went on saying that, even in case the current SIA regime were applicable, the arbitration clause should not have been upheld for two reasons:

- Firstly, because the parties had reached a partial settlement terminating the main agreement and therefore it was no longer possible to invoke the existence of an arbitration agreement;

- Secondly and most importantly, because "*the extraordinary extension of the common phase in this insolvency process and the fact that the process is currently at the arrangement phase, makes it desirable to have a joint and unified consideration of the economic issues that may arise […] [and], consequently, to submit the matter to the arbitrators might cause a damage to the insolvency proceedings"*.

Clearly there is a risk that this latter argument is used by insolvency courts to "neutralize" arbitration agreements relating to substantial economic disputes affecting the insolvency estate, for it is relatively easy to argue that having such an economic dispute subject to arbitration is more disruptive of the insolvency process than having it subject to the decision of the insolvency court.

In any case, one has to note that under the current SIA regime, ongoing arbitration proceedings involving an insolvent party cannot be suspended.