Dimitrov, Petrov & Co.
BULGARIAN LAW FIRM

Partners:
George Dimitrov
Bogdan Petrov
Alexander Todorov
Metodi Baykushev
Hristo Nihrizov
Zoya Todorova
Boyana Milcheva
Desislava Krusteva

Associates:
Dimitar Karabelov
Sylvina Beleva
Encho Simeonov
Donka Stoyanova
Emil Tumbev
Boyan Ivanov
Dimitar Benev
Bilyana Stefanova
Pavlina Ivanova
Gavrail Poterov
Pencho Stanchev
Tsvetelina Georgieva
Gergana Georgieva
Nikola Stoychev
Radina Tomanova
Martin Zahariev
Nikolay Kolev
Polya Donkova
Alexandra Lassina

Sofia 1303, Bulgaria
28 Todor Alexandrov Blvd,
fl. 7 and fl. 10
tel.: +359 2 421 42 01
fax: +359 2 421 42 02
e-mail: mail@dpc.bg

Varna 9000, Bulgaria
13 Neofit Bozveli Str,
office 13
tel: +359 52 694 505
e-mail: varna@dpc.bg

website: http://www.dpc.bg

MERITAS
LAW FIRMS WORLDWIDE

Could Bulgaria Have Avoided Payment under the Arbitral Award for Belene Nuclear Power Plant?

Martin Zahariev, Associate
Metodi Baykushev, Partner
Dimitrov, Petrov & Co.

Undisputedly the most significant event for Bulgaria for the past 2016 in the field of international arbitration is the issuance of the award under the case of the Russian company JSC AtomStroyExport (ASE) against Natsionalna Elektricheska Kompania EAD (National Electricity Company – NEK) concerning the order of equipment for building the nuclear power plant in Belene. According to the award, NEK was obliged to pay ASE around EUR 600 million. Consequently, the Bulgarian National Assembly adopted the Act for Granting Support for Payment of Debts of Natsionalna Elektricheska Kompania EAD (promulgated in SG, issue 76 of September 30, 2016) for the purpose of ensuring funds for NEK to voluntarily pay its debts to ASE. The total amount of the state loan to NEK for settling its relations with ASE was BGN 1.2 billion.

At present, the terms for legal defence have long expired, and the voluntary payment has already been made. Yet, the logical question arose: what were the options before NEK after the issuance of the arbitral award and was the voluntary payment unavoidable. In the present paper, this question will be answered by analyzing the options for legal defence against arbitral awards rendered under international commercial arbitration cases. It is impossible for external observers to "prescribe" what should and what should not have been done in these particular arbitration proceedings. A competent opinion could be given only by the lawyers who participated in the case and were familiar with all its details (including confidential information which was not publicly available). However, it is important to summarize the options for legal defence in arbitration proceedings in light of the case ASE against NEK so that in the future each option can be carefully examined in the light of the specificities of each individual case.

Arbitral awards are not subject to appeal

First, we should emphasise the fact that an arbitral award (in most jurisdictions around the world) is **final**. It resolves the respective legal dispute and may not be further appealed before another body (another arbitral tribunal, court, etc.). The traditional scheme of appealing before several instances which applies to court decisions is not applicable to arbitral awards.

…, yet arbitral awards may be set aside

This, however, does not mean that NEK, as the losing party in the case, was deprived of any opportunity to protect its rights. The first option available to NEK was to **request the setting aside of the arbitral award.** As the arbitral award finally resolves a particular legal dispute, the losing party should have some means to protect its rights in case of substantial defects in the issuance of the arbitral award. Those defects, in general, may affect the conclusion, scope and validity of the arbitration agreement, the procedure for formation of the arbitral tribunal and for hearing the dispute, etc. Such means for protection are the proceedings for setting aside an arbitral award. Setting aside applications may be filed only with the courts at the seat of arbitration, on the grounds and within the terms regulated by the national laws of the respective country where the seat of arbitration is.

In this case, two parallel proceedings were initiated between ASE and NEK - with different counterclaims between the parties. One of the proceedings had its seat of arbitration in Paris, and the other – in Geneva. Consequently, the parties agreed on joinder of the proceedings and on a seat of arbitration of the joined proceedings in Geneva. Therefore, an application for setting aside of the award should have been filed with the Swiss court on the grounds and within the terms provided for in the Swiss law.

The applicable Swiss act in the case is the Federal Statute on Private International Law (FSPIL). Pursuant to the relevant version of Art. 190 (2), letters 'a' – 'e' of FSPIL, an arbitral award may be set aside if:

- The sole arbitrator was improperly appointed or the arbitral tribunal was irregularly constituted;
- The arbitral tribunal has wrongly accepted or denied jurisdiction to hear the case;
- The arbitral tribunal has decided on issues which are beyond the scope of the submitted claims or has failed to decide on a particular claim;
- The principle of equal treatment of the parties or the rights of the parties to be heard were violated;
- The award is incompatible with the public policy of Switzerland.

The application to set aside is considered by the Swiss Federal Supreme Court. The term for filing a setting aside application is 30 days as of the notification of the award to the parties. Usually, the case is resolved relatively fast, which on average takes 4 months[1]. Due to the complexity of the case between NEK and ASE, the issuance of a decision on a setting aside application would most likely have taken more time. It should be noted that Swiss courts are arbitration-friendly. Nevertheless, the percentage of set aside arbitral awards in Switzerland

[1] Bärtsch, P., Schramm, D. Arbitration Law of Switzerland: Practice & Procedure, JurisNet, Huntington, New York, 2014, p. 81

is not insignificant (in the legal theory scholars made references to about 6.5 – 7% set aside awards[2]).

What is important in the case is that **the expenses in proceedings for set aside of arbitral awards in Switzerland are lower than in most jurisdictions**. For example, in proceedings with a value of the claim of CHF 1 million, the total amount of the court expenses and attorney fees for the losing party are usually up to 3% of the value of the claim or CHF 30,000. Increasing of the value of the claim entails decrease in this amount – in case of a value of the claim of CHF 10 million, the amount of expenses would be 0.3% of the value of the claim or about CHF 30,000 (See Swiss Setting Aside Proceedings: Quick, Reliable, and Arbitration-Friendly, Swiss Arbitration Association). **Therefore, with a value of the claim of USD 500 million, the amount of the expenses for conducting such set aside proceedings definitely would not have been a crucial factor.**

Applying for set aside of arbitral awards for large amounts of money is a common practice

Using the opportunity to apply for set aside of arbitral awards is a worldwide common practice, especially where high material interest is concerned. For example, the Russian Federation challenged six arbitral awards in the most widely discussed international arbitration case, which was initiated by the majority shareholders of Yukos (the former largest oil company in Russia) - Hulley Enterprises, Yukos Universal and Veteran Petroleum. Yukos' shareholders claimed that the Russian Federation has unlawfully expropriated their property. In this case Russia was ordered to pay the unprecedented in international arbitration amount of USD 50 billion, plus USD 60 million for attorney fees. Logically, Russia requested set aside of the six awards in the case (3 interim awards of November 30, 2009 and 3 final awards of July 18, 2014) before the court of the seat of arbitration - The Hague District Court. By a decision of April 20, 2016, The Hague court set aside the six arbitral awards, assuming that the arbitral tribunal was not competent to consider the dispute. At present, the case is appealed before the upper instance.

Analogically, Mexico requested setting aside of the arbitral award by which the national oil company of Mexico PEMEX was ordered to pay nearly USD 300 million to COMISSA, a subsidiary of the American construction company KBR Inc. The seat of arbitration was in Mexico, and a Mexican court was competent to hear the case. It is not a surprise for anyone that the Mexican company's request was considered well founded, and the award was set aside. Nevertheless, an American court subsequently enforced the set aside award (this is only the second set aside award subsequently enforced in USA for the past decades). Yet, this example shows how Mexico did not hesitate to use the set aside procedure as

[2] Bärtsch, P., Schramm, D. Arbitration Law of Switzerland: Practice & Procedure, JurisNet, Huntington, New York, 2014, p. 81; Dasser, F. International Arbitration and Setting Aside Proceedings in Switzerland: An Updated Statistical Analysis, 28 ASA Bulletin 82 (2010), p. 85-86

a means of legal defence against an arbitral award where the losing party is a state-owned company.

Egypt also requested setting aside of the award rendered in the arbitration proceedings against the English company Malicorp Ltd. In this case, Malicorp filed claims for lost profits amounting to USD 500 million and costs for over USD 12 million against the Egyptian government and two state-owned companies (the Egyptian Holding Company for Aviation and the Egyptian Airports Company). The case was initiated due to termination of a concession contract for design, construction and operation of an airport in Ras Sedr on the Red Sea. The arbitral tribunal found that it had no jurisdiction over the state-owned companies, but it ordered Egypt to pay USD 14,773,497 indemnification to Malicorp. The seat of arbitration was in Cairo. Not surprisingly, Egypt sought protection of its rights before the state courts in Cairo. The arbitral award was set aside by a decision of the appellate court issued in 2012, but the case is still being appealed before the Egyptian cassation court, which is another example of how states protect their interests by all possible means.

Bulgaria has also requested set aside of arbitral awards

Setting aside of arbitral awards rendered in arbitration proceedings with a seat of arbitration in Bulgaria has also been used as a means of protection by the Bulgarian state. Such an example is the case initiated by a German company against the Ministry of Environment and Waters (MEW), in which claims were filed under a contract for construction of 6 regional landfills co-financed by the Bulgarian government and the European Union under the pre-accession funds. The case was resolved in favour of the German company by an arbitral tribunal from the Arbitration Court at the Bulgarian Chamber of Commerce and Industry. Consequently, MEW filed a setting aside application before the Supreme Court of Cassation which was found justified on the grounds that the claims considered by the arbitral tribunal were different from the ones actually filed (Decision No. 59 of 06.10.2015 under commercial case No. 2/2015 of the Supreme Court of Cassation, 1st Commercial Division). **This is a clear example of a case in which the Bulgarian state effectively protects its rights by all possible means of protection.**

Even if the arbitral award is not set aside, not always shall the losing party pay

The second option which was available to NEK was the **legal defense against the enforcement of the arbitral award in Bulgaria**. If any foreign arbitral award is not voluntarily executed, the party that has won the case (in the present case ASE) has the option to seek assistance for its enforcement from the authorities of the state in which the debtor (in this case NEK) has assets. The idea is to impose the so called "execution proceedings" against these assets. The execution proceedings require the assistance of the competent authorities of the

state where the debtor's assets are located. Such assistance may be obtained only after this state recognizes the existence of the arbitral award. This is the very purpose of the procedure for the arbitral award enforcement.

A particular category of arbitration proceedings exists which does not require enforcement of the arbitral award. This is specific for the so called "investment arbitration" carried out pursuant to the Convention on the Settlement of Investment Disputes between States and Citizens of Other States (ICSID Convention)[3]. In investment arbitration under the ICSID Convention, the dispute is directly between the investor and the state where the investment has been made. The logic behind not requiring such enforcement is that the winning party shall not seek assistance for exercising its rights from the state with which it has a legal dispute, as it is quite possible for enforcement to be refused to this party. Therefore, pursuant to the ICSID Convention, its member states shall recognize the arbitral awards as if it were a final judgment of a court in these states.

The case between ASE and NEK is commercial arbitration – i.e. this is a dispute between two commercial companies, rather than between an investor and a state, although the beneficial owner of one of the companies is the Bulgarian state (as shown in NEK's annual financial report (AFR) for 2015 published in the Commercial Register, the sole owner of NEK is Bulgarian Energy Holding EAD, and the beneficial owner is the Bulgarian state through the Minister of Energy – page 61 of AFR), and the other one – the Russian Federation. In this sense, if NEK had refused to voluntarily pay its monetary obligations, enforcement of the arbitral award would have been necessary regardless of the state in which ASE intended to initiate execution proceedings.

Regardless of whether NEK has assets abroad (according to NEK's AFR for 2015, the company owns BGN 4,105,114,000 non-current assets, of which BGN 4,029,768 are real estates, machines and equipment, and there are no data whether some of them are located abroad – page 2 and pages 31-35 of AFR), it is logical to assume that NEK's largest assets are in Bulgaria. Therefore, for receipt of the amount of EUR 600 million it was logically expected that ASE would seek enforcement of the arbitral award namely in Bulgaria (and in case of any assets abroad – in the respective foreign country). It would put ASE in the **unfavourable position to seek enforcement of an award before the Bulgarian courts against the company whose beneficial owner is the Bulgarian state**.

<u>The last word could have been said by the Bulgarian court</u>

[3] It should be noted that there is no obstacle for investment arbitration to be carried out before an institution that deals with trade disputes – e.g. before the International Court of Arbitration of the International Chamber of Commerce in Paris (ICC), The London Court of International Arbitration (LCIA), etc., or before an arbitration set up for a particular dispute (the so-called *ad hoc* arbitration). In such case, however, the arbitral award would be subject to acknowledgement and admission to execution, regardless of having been issued under an investment dispute

Of course, the opportunity for legal defense in the enforcement proceedings of arbitral award is not unlimited. Much like the setting aside of the arbitral award, the grounds here are limited, as regulated in an international convention to which Bulgaria is a party – the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (also known as the New York Arbitration Convention of 1958). The grounds are regulated in Art. 5 of the Convention and, similarly to setting aside of the arbitral award, are related to defects in the conclusion, the scope and the validity of the arbitration agreement, the procedure for constitution of the arbitral tribunal and considering the dispute. Besides, grounds for refusal of the enforcement of an arbitral award are its subsequent setting aside and its being in conflict with the public order of the state where enforcement is sought. In Bulgaria, it is Sofia City Court that has jurisdiction to enforce a foreign arbitral award, and its decision is subject to appeal before Sofia Appellate Court and the Supreme Court of Cassation. In other words, NEK could have relied on three court instances to prove the existence of any of the grounds under Art. 5 of the New York Arbitration Convention, and thus to prevent the enforcement of the arbitral award in Bulgaria.

Internationally, seeking of legal defense against the enforcement of an arbitral award is frequently used by the losing party. For example, in 2011 in one of the landmark arbitration cases, Pakistan successfully prevented enforcement in the United Kingdom of an award for USD 20 million in favour of Dallah Real Estate and Tourism Holding Company - a travel company from Saudi Arabia. Pakistan challenged the existence of a valid arbitration agreement with Dallah, and ultimately the supreme court refused the enforcement on the grounds that the Pakistan government did not consent to arbitration.

Another example of preventing the enforcement is the case Malicorp Ltd. against Egypt. Although the case for setting aside the arbitral award was pending before the Egyptian Cassation Court, in 2015 Egypt successfully prevented the enforcement of the award in the United Kingdom. One of the arguments of Egypt was that the decision had been set aside by the Egyptian appellate court, and therefore it should not be enforced.

In Bulgaria, there are also examples of preventing the enforcement of foreign awards. **In 2004 enforcement was refused for an international arbitral award by which a Bulgarian company whose sole owner of the capital was the Bulgarian state was ordered to pay amounts under a contract in favour of a Kuwaiti company (Decision No. 630 of 28.07.2004 under civil case 1832/2003, Commercial Chamber, II Commercial Division of the Supreme Court of Cassation).** The arguments used by the Bulgarian court were based on the Kuwaiti company's missing the term agreed by the parties for filing a claim and on conflict with the public policy of the Republic of Bulgaria caused by depriving the Bulgarian company of the possibility to present all its arguments before the arbitral tribunal.

Of course, the opposite situation is also possible, in which the Bulgarian court enforces a foreign award against a Bulgarian company having its sole owner the Bulgarian state. Such is the case with Sofia Airport, which lost the case with a company having its seat in the United Arab Emirates before an arbitration tribunal in Paris. Subject of the case were claims for construction works and indemnifications for damages amounting to USD 20 million in total. The arbitral award was granted enforcement in two instances. Sofia Airport filed an appeal before the Supreme Court of Cassation, which did not admit the appeal to consideration, and thus the arbitral award was finally ruled enforceable in Bulgaria (Ruling No. 59 of 03.02.2017 under commercial case 788/2016, Commercial Chamber, I Division of the Supreme Court of Cassation).

Choosing one of the above options in each particular case is a matter of strategy. Both options could be and are often combined in practice, as far as it is logical for the debtor to exercise all its possible means of protection. The case NEK against ASE is already history. What is important, however, is to know that means of protection exist, and they could be used in order to avoid new large payments in arbitration cases.