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Disputable Aspects Regarding the Seat of Arbitration under Bulgarian Law

The identification of the seat of arbitration is undisputedly one of the most important features of an arbitration clause, as it determines *lex arbitri* and, consequently, which courts will have supervisory jurisdiction over the arbitration. According to Bulgarian law, the choice of seat of arbitration may also predetermine the possibilities for enforcement of an arbitral award. This view is supported in Article 117, Item 1 of the Bulgarian Private International Law Code (PILC). According to the said provision, the enforcement of foreign arbitral awards requires that a foreign tribunal should be competent under Bulgarian law. The current Bulgarian legislation, however, causes considerable disputes in relation to when an arbitral tribunal seated abroad is deemed competent to hear the dispute for the purposes of an enforcement procedure in Bulgaria.

The first significant issue is the general prohibition prescribed in Article 19, Paragraph 2 of the Civil Procedure Code (CPC). According to this rule, **arbitration between Bulgarian parties must be seated in Bulgaria.** Such strict and formal approach used by the Bulgarian legislator is likely to compromise the status of the arbitration procedure as a more convenient, cheaper, and more expeditious alternative to litigation.

Actually, state litigation procedures in cases with an international element may turn out to be more business-orientated. For instance, pursuant to Article 7 of the Council Regulation (EU) No 1215/2012, any specific element of an international relationship, such as place of performance of obligation, place of occurrence of a harmful event, etc. may be deemed relevant for the establishment of forum competence. Furthermore, Article 25 of the Regulation provides for a "*prorogation of jurisdiction*", meaning that the parties to a legal relationship with an international element may agree on jurisdiction of certain Member State court/courts.

In contrast to the European law, the Bulgarian legislation seems not to take into consideration the separate elements of the international relationship as a precondition for the arbitration to be seated abroad, but rather prefers to preserve the conservative approach.

The second significant issue is the interpretation of Article 19, Paragraph 2 of the CPC in light of the admission of setting the arbitration abroad. The latter is

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possible only in case *"one of the parties has its* ***habitual residence***, ***seat*** *according to its statutory acts or* ***place of actual management*** *abroad".* The cited terminology, however, is rather ambiguous, especially the phrase "*place of actual management*". According to the international private law doctrine (the so called theory of the control or "real seat doctrine"), the term could refer to different concepts in different Member States, such as the meeting place of the board of directors, the location of the general meeting of the shareholders, etc. [See for example Cynthia Day Wallace, *The Multinational Enterprise and Legal Control.* Martinos Nijhoff Publishers, 2002]. It is quite uncertain which interpretation would be followed by Bulgarian courts.

The matter becomes even more complicated with a view to analogous connecting factors in other Bulgarian legislative acts. The International Commercial Arbitration Act (ICAA) introduces slightly modified terms "***residence***", "***seat***", and "***predominant foreign participation",*** none of which is defined in the ICAA. According to the ICAA, the first two connecting factors are sufficient to agree on the seat of arbitration abroad. The third one, however, as prescribed by Paragraph 3 of the Transitional and Final Provisions of the ICAA, can justify only the choice of an arbitrator from a different country but not the choice of arbitration seated abroad.

The PILC increases the ambiguity further by using the terms *"habitual residence"*, *"headquarters under its articles of association"* and *"location of actual management"* as grounds for Bulgarian courts' jurisdiction.

In contrast to the terms used in Bulgarian legislative acts, Article 63 of the Regulation No 1215/2012 states that legal entities are domiciled at the place where they have their statutory seat, central administration, or principal place of business. According to the Bulgarian legal doctrine, the statutory seat stands for a more formal criterion, whereas the other connecting factors are rather factual and corresponding to the variety of business activities [See Nikolay Natov, et al., *Regulation Brussels I Commentary,* Ciela, 2012, pp. 570-571]. Thus, it is evident that the European legislator uses not only formalised criteria to link a legal entity to a certain country. It has to be acknowledged that the ICAA makes an attempt to follow this European model by using "*predominant foreign participation*" of a legal entity as a precondition for the appointment of a foreign arbitrator. Nonetheless, the meaning of the term is not absolutely clear.

The Bulgarian case law has made some endeavours to clarify the raised issues. However, at least for now only a limited number of relevant arbitral and court decisions have been issued. According to Ruling No 2368/2012 under case No 3963/2012 of Sofia Court of Appeal, **the fact that the sole manager of a limited liability company – a party to an arbitration agreement – has**

his/her habitual residence outside Bulgaria is enough to ensure the validity of the agreement for having arbitration seated abroad.

The interpretation made in this court decision also raises many questions, especially in cases where the management bodies of the entities consist of several members domiciled in different states. It is unclear whether the relevant criteria would refer to the location of one or of the majority of the Board members. The ambiguity extends further if the members of the management bodies are legal entities, which is possible for joint-stock companies under the Bulgarian Commercial Act In such cases, the managing legal entity appoints a representative (a natural person) to represent it in the management body. It is unclear whether the domicile of the representative or of the entity Board member should be deemed relevant.

The other unclear issue is about the relevant moment in time towards which the predominant foreign participation has to be considered – i.e. should that participation be present at the time of conclusion of the arbitration agreement or at the time of commencement of arbitration?

Therefore, it would be risky for two Bulgarian entities to agree on arbitration seated abroad even if their managers are not domiciled in Bulgaria. If these managers are later replaced by managers domiciled in Bulgaria or the abroad seated entities appoint Bulgarian representatives in the management body, the Bulgarian court may find that the arbitration clause null and void due to contradiction with Article 19, Paragraph 2 of the CPC. As a result, the enforcement of the arbitral award rendered abroad may be refused.

The third significant issue with regard to having arbitration abroad arises in multi-party arbitration: if a dispute involves simultaneously three parties – e.g., one Bulgarian-based entity, and a Bulgarian and foreign entity which are jointly liable. Such situation is likely to occur in cases where a Bulgarian company is a subsidiary of a foreign corporation. In this case, if only one of the respondents has its registered address abroad, it is questionable whether arbitration abroad would be in compliance with Bulgarian law as the court practice is not consistent on this matter.

According to the Ruling No 106/2012 in the case No 65/2012 of the Varna Court of Appeal, the parties to multilateral contracts can agree to have the arbitration seated outside Bulgaria if at least one of the parties has its registered address abroad. However, in such cases, this can be done only with regard to the disputes arising out of the relations with that party registered abroad.

A different conclusion regarding multi-party arbitration was drawn in the Ruling No 2131/2014 in the case No 2697/2014 of the Sofia Court of Appeal (still pending case). According to the arbitration clause in the case, a Bulgarian entity (respondent) was jointly liable with a guarantor seated abroad. The clause

provided that both the respondent and the abroad-seated guarantor shall be considered one party for the purposes of the arbitration and shall be represented by the same lawyer. The court ruled out that in such case the arbitration agreement may provide for the seat of the arbitration abroad. The court even asserted that the claimant may not avoid the agreement by filing a claim only against the Bulgarian respondent, thus preventing the guarantor from making an objection against the state court competence. All the parties are bound by the agreement, and the claimant should file its claim against both the respondent and the guarantor before the arbitration tribunal (seated outside Bulgaria).

In conclusion, all the described ambiguities of the Bulgarian legislation, together with the inconsistencies and the lack of case law, result in practical difficulties and uncertainties for both Bulgarian and foreign contractors when designing their arbitration agreements. It can be inferred that a valid and enforceable foreign arbitral award may be guaranteed only in a simple scenario when there are two parties to a contract and at least one of them has its registered address outside Bulgaria, regardless of its actual management. In any other case, the final outcome of having arbitration seated abroad would depend to a great extent on the precise formulation and interpretation of the arbitration clause. Hopefully, Bulgarian courts will provide the necessary clarifications on these issues, in order to make Bulgaria a more attractive jurisdiction for both domestic and foreign investors.

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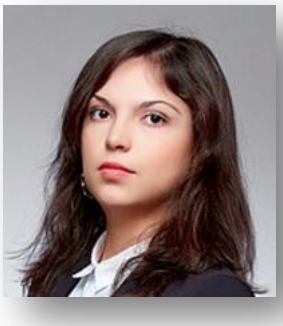

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