Israeli Arbitration Law in Knots? Foreign Service of Process for 'Made in Israel' Awards

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On 31 December 2017, Israel's Supreme Court published an important precedential decision concerning enforcement procedures of 'made in Israel' commercial arbitral awards. In Request for Appeal 1739/17, ***Michael Flacks v. Stephan Bisk*** *(in Hebrew),* the Israeli Supreme Court denied a motion for service of process abroad in a petition to confirm an arbitration award issued in Israel. The court held that Israeli courts should generally not exercise "long arm" jurisdiction on a foreign party just because the arbitration was seated in Israel.

In this post, we will first present the material facts of the case and explain in a nutshell the legal basis for the decision: the Israeli Arbitration Law 5728-1968 ("**Arbitration Law**") and the relevant provisions of the Civil Procedure Regulations 5744-1984 [consolidated version] ("**Civil Procedure Regulations**"). Then, we turn to discuss the majority opinion as well as the dissenting opinion in reference to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) (**"New York Convention**") and the UNCITRAL Model law on International Commercial Arbitration 1985: with amendments as adopted in 2006 (("**Model Law**"). We conclude with the problematic result that this precedent generates.

The Material Facts of the Case

The parties, Bisk – an Israeli resident and a US citizen, and Flacks – British citizens and US residents, entered into a commercial agreement, according to which Bisk paid a sum of 300,000 USD to Flacks, designated for a property investment in Germany. The agreement included an arbitration clause, providing for arbitration of disputes in Beit Din in Israel (Beit Din is an institutional arbitration court based on Jewish law). When the debt matured and Flacks did not return the principal nor the premium, Bisk initiated arbitration proceedings in Israel. Flacks argued that the arbitration agreement was not valid since the parties reached subsequent agreements that effectively cancelled the arbitration clause. The arbitration panel ultimately appointed dismissed Flacks' jurisdictional objections arguments and ruled in favor of Bisk in two subsequent arbitration awards: one concerning the principal sum and the latter concerning the premium.

Pursuant to the Arbitration Law, Bisk then applied to the Israeli court for confirmation of the arbitration award. Since Flacks does not reside in Israel, Bisk submitted a motion for service of process abroad. Both the registrar at the District Court, and on appeal, the judge, granted permission for service of process abroad. However, on a request for appeal to Israel's Supreme Court a majority

ruling overturned this decision and denied the motion for service of process abroad.

The Legal Basis for the Decision

As background for presenting the reasoning for this decision, it is important to understand the Arbitration Law and the Civil Procedure Regulations that apply to service of process abroad. Under the Arbitration Law, an arbitration award does not require judicial confirmation. However, according to Article 23 of the Arbitration Law, if a party wishes to enforce the award via the Enforcement and Collection Authority (the judicial branch that administers collection of debts and obligations) it must apply for judicial of the award (**"Confirmation Proceedings**"). The Confirmation Proceedings requires notice to be given to both parties' (not an ex-parte proceeding). Essentially, if the respondent is a foreign party, service of process abroad must first be undertaken.

The rules that generally apply to permitting service of process abroad to a foreign party are rooted in the Civil Procedure Regulations and extensive case law. These rules require three cumulative conditions: (a) the cause of action is listed in the closed list of causes in regulation 500 of the Civil Procedure Regulations ("**Regulation 500**"); (b) there is a good and substantiated cause of action against the respondent; and (c) Israel is a convenient forum.

The majority reasoning – a narrow interpretation of Regulation 500

The causes of action listed in Regulation 500 all demonstrate either a personal connection of the respondent, or a subject-matter connection of the case, to the State of Israel. Courts have consistently held that international comity considerations lead to a narrow interpretation of Regulation 500.

In Flacks, the District Court approved the service of process abroad based on subsection (4) of Regulation 500, which permits extension of jurisdiction in disputes relating to contracts that were either made in Israel or are subject to the laws of Israel. The district court held that the arbitration agreement, that was part of the commercial agreement between the parties, and which designated Israel as the seat of the arbitration, suffices for such purpose.

In accepting the appeal, the Supreme Court held that an action to confirm the arbitration award is *distinct* from the action based on the agreement between the parties. At the post-award stage, Confirmation Proceedings are no longer an action based on the arbitration agreement, but rather stem for the arbitration award. Accordingly, Subsection 500(4), based on a contractual claim, cannot create the basis for summoning a foreign respondent. The majority verdict summarized that the mere fact that a court is asked to confirm a 'made in Israel' arbitration award, is not sufficient for creating personal jurisdiction over the foreign respondent, since award confirmation is not a contractual cause of action.

The Dissenting Opinion and New York Convention

Subsection (8) of Regulation 500 allows overseas summons for enforcement of 'foreign arbitral awards as defined in the Arbitration Law' while Confirmation Proceedings (even of foreign awards) are not explicitly listed. The dissenting opinion suggested filling this legal lacuna by assuming that the Israeli legislator did not want to treat Israeli arbitration awards as inferior to foreign awards, and construing Subsection (8) to include Confirmation Proceedings. The majority opinion however expressly dismissed such an expansive construction of Regulation 500, considering international comity.

In this context it is important to note the different scope of application of the New York Convention, the Model Law and the Arbitration Law. Article 1 of the Arbitration Law distinguishes between 'foreign

and ‘domestic’ awards, defining a foreign arbitral award as an award ‘made outside Israel’. The scope of application of the New York Convention covers, according to Article 1 of the Convention, both **awards made outside the State** where the recognition and enforcement are being sought, and **awards not considered domestic**. The Arbitration Law does not recognize any award made in Israel as not being domestic, regardless of the parties or circumstances involved, so the second option under the New York convention is not reflected in local law.

Interestingly, the Model Law specifically clarifies (e.g. in Articles 1(2) and 35) that recognition proceedings can be made irrespective of the country in which the award was made if the award is not considered domestic. Thus, in the event that the arbitration involves international elements, such as the case was in Flacks, according to the model law this may fall under the definition of international arbitration. Since the Arbitration Law, which predates the Model Law, and the Civil Procedure Regulations, distinguish, for the purpose of service of process, between foreign and domestic awards, the outcome in *Flacks* is different than the outcome that would have been reached had the Model Law and appropriate regulations been adopted by the Israeli legislator.

Israeli Supreme Court Ties the Arbitration Law Up in Knots

Despite the undesirable result and troubling outcome expressly noted by the Supreme Court, *Flacks* set a precedent that Israeli courts will not extend their jurisdiction to foreign parties merely because the arbitral award is made in Israel. At the same time, Israeli courts will extend jurisdiction to foreign parties in enforcement procedures of awards not made in Israel and that are subject to the New York Convention. Consequently, arbitral awards rendered in Israel cannot be confirmed by an Israeli court and enforced in Israel if the foreign party objects to jurisdiction and there are no other causes of action that allow the service of the process abroad. This problem may be solved by initiating enforcement and recognition procedures in the foreign jurisdiction pursuant to New York Convention, as suggested by the Supreme Court itself. Since, as the majority opinion noted, this problematic outcome can only be fully resolved by a future amendment to the Civil Procedure Regulations, parties choosing arbitration in Israel are advised to note this procedural hurdle and act according to it when drafting arbitration clauses.