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An Ex-Yugoslav Odyssey: A Metamorphosed Arbitration Agreement and an Arbitral Institution that Ceased to Exist

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Saturday, September 28th, 2019

In 2012, the Commercial District Court in Bijeljina ('CDC') finally declared that it lacked jurisdiction to hear the dispute between *Elektrogospodarstvo Slovenije* ('Claimant') on one side, and *Rudnik i termelektrana Ugljevik A.D.* ('Respondent') on the other (Case reference no. 59 0 Ps 018507 12 Ps 3), with the High Commercial Court in Banja Luka ('HCC') affirming the decision of its lower counterpart.

The CDC declined jurisdiction based on the fact that the Self-Governance Agreement 1 and the Self-Governance Agreement 2 ('Agreements') under which the dispute arose called for arbitration as a mechanism for settling legal controversies between the involved parties. This, in and of itself, would hardly be an interesting topic for a discussion. However, the process of disintegration of the Socialist Federal Republic of Yugoslavia ('Yugoslavia') at the beginning of the 1990s has brought about two aspects that make this case a rather thought-provoking material for both scholarly and practitioners' debate. Firstly, the parties, in case of any dispute under the Agreements, called for arbitration under the auspices of the Electric Power Industry of Yugoslavia ('EPIY'), an institution that ceased to exist before the arbitration agreement could be consummated under its auspices. Secondly, at the time the Agreements were concluded (in 1981 and in 1988 respectively), both parties were Yugoslav legal entities whereas at the time their dispute came before the CDC Bijeljina, they were two entities seated in different countries (the Claimant in Slovenia, and the Respondent in Bosnia and Herzegovina ('BiH')).

This post will first briefly summarise the facts of the case. Then, it will elaborate on the CDC's and HCC's reasoning in upholding the arbitration agreement between the Claimant and the Respondent, with the focus being on the two rather intriguing issues (mentioned above). And last but not least, the post will offer critical analysis of the approach taken by the CDC and the HCC.

Factual Background

The Agreements anticipated that the Claimant would invest substantially in the

construction and operation of a thermal power station *Ugljevik* on the territory of what was then the Socialist Republic of BiH, a constituent part of Yugoslavia. In exchange for its investments and participation in the project, the Claimant was, as per the Agreements, entitled to one third of the electrical energy produced in the thermal power station *Ugljevik*. However, the transmission of the electrical energy from the thermal power station *Ugljevik* was stopped in 1991, and as a consequence of the bloody conflict and the ensuing dissolution of Yugoslavia, it was never resumed. In the late 2000s, the Claimant sought to enforce the substantive provisions of the Agreements by initiating a case before the CDC that, eventually, and as already noted, declined jurisdiction owing to the existence of an arbitration agreement between the parties to the dispute.

Selected Aspects of the CDC's and HCC's Reasonings

The underlying question before the CDC Bijeljina was the following one: Is the arbitration agreement between the Claimant and the Respondent enforceable in the case at hand? The CDC answered this question in the positive, and the HCC affirmed its decision. In reaching this conclusion, the CDC relied on Article II of the New York Convention and on the relevant provisions of the applicable Code of Civil Procedure.

As for the fact that the institution under whose auspices arbitration was supposed to take place no longer existed, the CDC did not find this to be detrimental for the arbitration agreement between the Claimant and Respondent. It supported its stance by noting that the EPIY was not an arbitral institution with its set of arbitration rules. Instead, arbitration that was to be conducted under its wing was not institutional but practically of *ad hoc* character. Consequently, in the view of CDC, even after the termination of the EPIY, the arbitration agreement between the Claimant and Respondent remained unscathed. The parties still could arbitrate their dispute in an *ad hoc* manner.

In the appeal before the HCC, the Respondent raised the issue of what can be vividly described as a metamorphosis of the arbitration agreement between them and the Claimant from one that envisages domestic arbitration to one that, if triggered, would produce arbitral proceedings of an international character. The Respondent emphasised that at the time the Agreements were concluded, the parties did not foresee that Yugoslavia would disintegrate, with this unfortunate occurrence, in effect, turning any dispute between them to one that is international in its nature. The HCC did not really address this argument, with the closest notion that it put forward in this regard being an observation that arbitration is a creature of consent that stems from the free will of the parties. Since the parties never terminated their arbitration agreement, it still possesses a legal effect to substitute the jurisdiction of the courts.

Could Pendulum Have Swung the Other Way?

Whatever their motivation, one could characterise the approach taken by the CDC and the HCC as being remarkably pro-arbitration in the case at hand. This is even more

astonishing given the fact that BiH is certainly not known as a pro-arbitration jurisdiction. At the same time, however, the arguments that the case ought not to proceed to arbitration are certainly not without merit.

Namely, Article II(3) of the New York Convention calls for courts to refer the parties to arbitration if one of them so requests unless the arbitration agreement is "null and void, inoperative or incapable of being performed". In the case at hand, it is indeed a thought-provoking issue whether the arbitration agreement is indeed capable of being performed. One glimpse into the case law rendered under the New York Convention reveals that several courts in different jurisdictions have found that the non-existence of an arbitral institution at the time of the dispute renders the arbitration agreement as incapable of performance.[1)] This seems to be the approach implicitly followed by the CDC and HCC. They have concluded that, since the EPIY lacked characteristics of a conventional arbitral institution (e.g., they did not have their arbitral rules in place), the parties have not, in reality, opted for institutional, but rather *ad hoc* arbitration. Thus, had they opted for a more traditional arbitral institution, and then this one ceased to exist, the two Bosnian Courts would have found the arbitration agreement to be incapable of performance.

This approach is not without its fair share of difficulties. The EPIY, while perhaps not being a conventional arbitral institution, had the capacity to administer arbitral proceedings, and other contracts in the energy sector in Yugoslavia concluded between other legal entities often called for arbitration under its auspices.[2)] As rightly pointed out by the Claimant, during the period when the Agreements were concluded with the Respondent, arbitration under the EPIY's wing was a natural choice as it was in line with the prevailing social and economic circumstances of that time. The EPIY, in essence, was in charge of ensuring uninterrupted functioning of the electric utility sector in Yugoslavia.[3)] Thus, it undoubtedly was in a unique position of having first-hand authority and expertise to deal with the disputes such as the one that arose between the Claimant and the Respondent. By sending the parties to arbitrate, the CDC and HCC have, no more and no less, imposed something that bears no resemblance to what was initially agreed upon in the arbitration agreement. This result seems hardly reconcilable with the universal notion that arbitration is the creature of consent.

Another interesting aspect of the case at hand is the unintended transformation of the arbitration agreement from the one that foresees domestic arbitration into one that generates international arbitration. The HCC, as already noted, did not find this aspect to be the least bit problematic. However, it ought to be noted that domestic arbitration is generally considered as quite a different animal as compared to international arbitration. Thus, one can often read the scholars referring to domestic arbitration regime on one hand, and international arbitration regime on the other.[4)] Even when a country regulates domestic and international arbitration in the same piece of legislation, in practice, important differences do exist. For instance, the latter generally brings into play the New York Convention which usually does not occur in relation to the former. Moreover, in some UNCITRAL Model Law jurisdictions, it was held that "international arbitration agreements must be upheld even in circumstances

where a comparable domestic arbitration clause would not be".[5)] Taking all this into account, it is rather lamentable that this issue was not given more importance in the decision-making process of the HCC.

What Has Happened Since?

Two arbitral proceedings have been unfolding: an investment arbitration *versus* BiH under the auspices of ICSID (ICSID Case No. ARB/14/13), and an international commercial arbitration of *ad hoc* character in Belgrade, Serbia. The former has been initiated by the Claimant based on the Bilateral Investment Treaty that Slovenia and BiH signed in 2001, and on the Energy Charter Treaty. As for the latter, the Claimant sought that these proceedings be stayed until the investment arbitration in front of the ICSID tribunal is brought to an end. As of this date, neither arbitration has resulted in an award, and the information that is publicly available remains scarce.

References

↑1 For a succinct analysis and overview of case law that deals with the dissolved arbitral institutions in relation to Art. II(3) of the New York Convention, *see* S. Kröll, "The 'Incapable of Being Performed' in Article II(3) of the New York Convention", in E. Gaillard and D. Di Pietro, 2008. *Enforcement of Arbitration Agreements and International Arbitral Awards: The New York Convention 1958 in Practice*, Cameron May: 332-335.

↑2 For example, in a contract regarding the nuclear power plant *Krško*, the Croatian side and the Slovenian side called for arbitration under the auspices of EPIY. Svetlana Vasović-Mekina, 2000. "Beograd, arbitar". Vreme, 517.

↑3 Law on Association into the Electric Power Industry of Yugoslavia, 18/78. *Official Gazette of the Socialist Federal Republic of Yugoslavia*.

↑4 *See* G. Carducci, 2012. "The Arbitration Reform in France: Domestic and International Arbitration Law". *Arbitration International*, *28*(1), pp.125-158.

↑5 G. Born, 2014. *International Commercial Arbitration*. Kluwer Law International: 644-645.