Kluwer Arbitration Blog

Georgia – Positive Changes in the Caucasus Region?!

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In 2009, Georgia adopted a new Law on Arbitration ("Law on Arbitration") based on the UNCITRAL Model Law on International Commercial Arbitration with amendments as adopted in 2006 ("Model Law"). Shortly thereafter, Mr. Michael Wietzorek commented on the implementation of the new law on the Kluwer Arbitration Blog (here) and qualified this as a "significant step for the further development and promotion of international commercial arbitration within the Republic of Georgia and the entire Caucasus region." Recently, the Law on Arbitration was further amended based on the bill proposed by the Ministry of Justice, enacted on 18 March 2015 ("Bill of Amendments"). The legislative intent behind the amendments was to eliminate the existing gaps in the law to increase its efficiency.

Some of the Key Amendments

1. Definition and Form of Arbitration Agreement. The Law on Arbitration adopted to a large extent Article 7 Option I of the Model Law in defining an arbitration agreement and its form. The Bill of Amendments abolished strict form requirements applicable when both parties to an arbitration agreement are natural persons. The repealed provision required signature to an arbitration agreement by parties' counsels in addition to the parties themselves, or in alternative, the notarization of such arbitration agreement. This rule was redundant from the moment of its adoption due to the existence of another consumer protection mechanism contained and still existing in Article 8(8) of the Law on Arbitration. The latter requires that the arbitration agreement is made in writing in the form of a document, and signed by the parties, when at least one party to such an arbitration agreement is a natural person or an administrative body. Neither electronic form nor exchange of statements of claim and defence suffices. Whilst strict form requirements for arbitration agreements for the consumer protection purposes are not unusual, it remains uncertain what legitimate interest the Georgian legislator seeks to protect when imposing such form requirements for arbitration agreements involving administrative bodies.

While the current amendments do not concern the substantive validity of arbitration agreements, the Georgian courts' precautious interpretation in this regard is noteworthy. According to case law, an enforceable arbitration agreement should explicitly determine the subject matter of the arbitration and should refer to an institution identifiable to the court. The latter prerequisite is interpreted narrowly. As an example, in an unreported case from November 2014, the court declared an arbitration agreement invalid because the address of the institution, being also the place of arbitration, referred to in the arbitration agreement was different from the address of the arbitral institution which seized of the matter by the claimant in that dispute. Therefore, it must be

concluded that Georgian courts do not have a pro-arbitration approach giving preference to the parties' intent to arbitrate, but rather construe arbitration agreements strictly.

2. Possibility of an *Ad Hoc* Arbitration. The previous adoption of the law compelled the parties to an arbitration agreement to agree on the rules of an arbitration institution. This fundamentally limited parties' freedom to have their case decided in *ad hoc* arbitration, and establish their own rules of procedure. The current version of the Law on Arbitration stipulates that the "*parties may agree on the rules of arbitration proceedings*" without further referring to the rules of an arbitration institution. This way, Georgian arbitration law now permits and recognizes *ad hoc* arbitration, and thus aligns with the Model Law. This amendment gives organized and cooperative parties the flexibility to resolve their disputes in a less expensive and less bureaucratic manner. However, the effectiveness of introducing ad hoc arbitration still has to be seen in light of the courts' narrow interpretation of arbitration agreements. Courts should alter their approach, as discussed above, and encompass *ad hoc* arbitration as well.

3. Arbitration Agreements and Substantive Claims Before Courts. The amendment related to substantive claims before state courts has been fuelled by Article 8 of the Model Law. Under Article 9.1 of the Law on Arbitration, courts are compelled to terminate proceedings and refer the parties to arbitration when the following cumulative conditions are met:

(a) The subject matter of the dispute falls within the scope of an arbitration agreement that is not null and void, inoperable, or incapable of being performed (substantive condition). Before the current amendments, parties were required to notify the court on the substance of the dispute subject of an arbitration agreement. This requirement has been repealed. Such change could be considered as a legislative will to promote state courts to adopt a prima facie approach rather than to fully review the validity, operativeness, performability, and enforceability of an arbitration agreement. Whether this will be put in practice is yet to be seen.

(b) Parties' referral to arbitration should be made no later than the submission of the Statement of Defence (procedural condition). As opposed to the previous adoption of the Law on Arbitration, the existence of parallel arbitral proceedings is no longer a prerequisite.

4. Competence-Competence. The Law on Arbitration recognizes an arbitral tribunal's competence to rule on its own jurisdiction. However, before the current amendments, such competence did not extend to ruling on whether the tribunal was exceeding its authority. The law simply did not govern this matter. As a result, parties had to resort to state courts in order to challenge a tribunal exceeding its scope of authority. The Law on Arbitration now aligns Georgian arbitration law with Articles 16(1) and 16(2) of the Model Law. Furthermore, the Law on Arbitration also subjects the tribunal's *competence-competence* to a subsequent court review, while eradicating the flaw existing in the Arbitration Law in terms of a court's power to make a final ruling on the jurisdictional question. Previously, Article 16(5) of the Law on Arbitration stipulated that if the tribunal decided on its competence, parties had to bring this matter to court within thirty days. It did not specify, however, whether the decision was to be made in a preliminary ruling or in a final award. Critically, it left open as to which of the two instances the thirty-day period applied. This ambiguity in the language created leeway for an interpretation that a thirty-day challenge period could apply for challenging the tribunal's decision on its jurisdiction rendered with a final award. Naturally, this interpretation leads to a direct conflict with the rules of setting aside of a final award, entailing a much longer, ninety-day period for commencing such proceedings. As a result of the Bill of Amendments, the Law on Arbitration clarified that the tribunal is authorized to rule

on a plea that it does not have or is exceeding its competence, *either* as a preliminary matter *or* in a final arbitral award, and that parties are authorised to challenge such preliminary ruling within thirty days. Also, the law explicitly authorises parties to decide in which manner they wish the tribunal to render their jurisdictional decision. Retrospectively, this can be an interesting development for an ongoing debate whether the failure to raise objections against the tribunal's preliminary ruling precludes further challenges in setting aside or enforcement proceedings (posts on this available here and here). If the parties agree that they wish the tribunal to rule on a jurisdictional plea in a preliminary award, i.e. at an early stage of the proceedings, this may give another argument for an interpretation that the parties consented to avoid disruptions regarding jurisdiction at any later stage of the process, including the means of challenging the final award or resisting enforcement on this matter.

5. Setting Aside and Enforcement of Awards. Following the structure of the Model Law, the Law on Arbitration contains separate articles dealing with the setting aside of an award (Article 42) and the recognition and enforcement of an award (Article 45). While the former deals with awards rendered on the territory of Georgia, the latter concerns the recognition and enforcement of awards irrespective of the country in which they were made. Notably, for the first time, the law unequivocally stipulates that an application for setting aside (Article 42(1)) is the sole recourse against an award. Furthermore, grounds for setting aside and denying recognition and enforcement of arbitral awards mirror the grounds listed in Article 34(2)(a) and (b) and Article 36(1)(a) and (b) of the Model Law, with some minor differences. First, in addition to the incapacity of a party to the arbitration agreement, Article 42(2)(a.a) and Article 45(1)(a.a) allow a party under some incapacity to have a legal guardian with regard to the issues under the arbitration agreement. If such support from a legal guardian is not received in relation to the arbitration agreement, this becomes a ground for setting aside and refusing to recognize and enforce an award. Second, before the amendments of 2015, improper notice to a party of the appointment of an arbitrator, or of the commencement of arbitral proceedings, or the inability to participate in the proceedings "*due to other valid reasons*" was a ground for setting aside an award and for resisting recognition and enforcement. The legislator has abolished this ground due to its ambiguity and instead introduced the language of the Model Law: "*or was otherwise unable to present his/her case*" (Article 42(2)(a.b)).

In terms of the recognition and enforcement of awards, one cannot avoid discussing the practice of state courts in this regard. Georgian courts frequently interpret their role as an "appeal instance" and lean towards an extensive interpretation of public policy. Courts have denied the recognition and enforcement of awards for violation of both procedural as well as substantive public policy, using a broad interpretation. To name but a few: lack of reasoning by the arbitrators in the award, awarding high penalties to one party, signature to the arbitration agreement only by one party, inability to participate in the proceedings [Judgment of the Supreme Court of Georgia (case no.: ?-2344-?-67-2014), dated 22 October 2014] have been some of the examples of the courts' broad interpretation of public policy. Clearly, even when courts have a specific rule to apply (e.g. invalidity of arbitral agreements, due process), they tend to resort to public policy. Regrettably, Georgia is still far from falling in the same bucket as the "vast majority of jurisdictions" adopting a narrow interpretation of public policy.

Nonetheless, it must be said that the current amendments eliminated an important legal flaw, by virtue of which courts looked at the conflict of arbitral awards with public policy. Now, courts are to discuss whether the recognition and enforcement of a certain award and not the award itself is in conflict or in conformity with public policy following the wording of the New York Convention as well as the Model Law. We can only remain positive that this amendment may change the courts'

attitude.

Conclusion

The legislative decision to modernize the Law on Arbitration is clearly an encouraging progress in shaping Georgia as a pro-arbitration jurisdiction. The revisions of 2015 eradicated some of the obvious legal flaws. However, a long way towards becoming an arbitration-friendly jurisdiction still lies ahead. The ball is now in the court of judges applying the law. If not given effect by courts, any amendment will only stay as a mere technical fix in the legislation. Recognizing tremendous efforts in conducting training programs for judges through various international projects, the local bar and the judiciary chapter of the ICCA, and having observed the Georgian legislator's pro-activeness, we should remain optimistic that Georgian courts will change their approach and follow the footsteps of successful arbitration jurisdictions.

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