Kluwer Arbitration Blog

Arbitration Tribunals' Curtailed Jurisdiction in Armenia: Again "No" to the Contract Invalidity Issue

Mushegh Manukyan (Office of the Ombudsman for United Nations Funds and Programmes) · Tuesday, November 19th, 2019

More than four years have passed since the Armenian Cassation Court—the highest court in Armenia—held in its EKD/1910/02/13 (2014) decision ("Cassation Court Decision") that *only state courts may exercise jurisdiction over the issue of contract invalidity* (see previous post). To recall, the Cassation Court reasoned that civil rights could be protected through judicial, administrative or public (arbitration) means but that "*the most guaranteed option was the judicial option because in such case the protection was conducted in accordance with the judicial procedure strictly envisaged by the law…*" To that end, given the importance of civil rights concerning contract invalidity, the Cassation Court found that those rights shall be protected by state courts rather than by arbitral tribunals. The Cassation Court Decision had a limiting effect on the scope of arbitrable issues and thus paralyzed the Armenian arbitration system.

Following this decision, the Parliament amended the Civil Code in 2015 by specifically stipulating that "[t]he protection of civil rights is provided by a court *or arbitral tribunal*…" (the "2015 Amendment"). The policy justification that the government put forward to amend the Civil Code was by reference to the Cassation Court Decision, making clear that it limited "the possibility of resolving disputes arising from certain legal relationships through arbitration." However, despite the 2015 Amendment, the court practice of rejecting the jurisdiction of arbitral tribunals over the contract invalidity issue appears to remain intact.

2019 Civil Appeals Court Decision

A recent decision of the Civil Appeals Court dated 16 April 2019 in the KD2/0548/02/18 case signalled that the Armenian courts would continue limiting the ability of arbitration tribunals to exercise jurisdiction over the contract invalidity issue. In this dispute between two major telecom companies, the claimant sought damages arising out of the invalidity of a 2009 contract in a state court despite the fact that the contract contained an arbitration clause. The court, however, agreed with the respondent that sought to stay the proceedings, relying on the arbitration clause. The claimant subsequently appealed the court decision before the Civil Appeals Court, relying, *inter alia*, on two main grounds:

First, it argued that the 2015 Amendment does not affect a contract concluded in 2009;

Second, the claimant also asserted that with the 2015 Amendment the legislature targeted only employment, consumer, and family disputes.

The Appeals Court held that the contract invalidity issue shall be exclusively decided by state courts. The decision was appealed to the Cassation Court, but the appeal was subsequently dropped. The Appeals Court's decision appears to be premised on the proposition that the contract invalidity issue is so important that it cannot be entrusted to arbitral tribunals. The Appeals Court, citing the Cassation Court Decision, reiterated that the State has an obligation to create "necessary and effective mechanisms" to ensure that the right to effective means for legal protection can be fulfilled "fully and effectively." In light of the Cassation Court's statutory powers to ensure the interpretation and uniform application of laws, the Appeals Court deemed that the Cassation Court Decision had already specified instances of specific importance that shall be decided by state courts. To that end, the Appeals Court held that the dispute at hand "shall be subject to the first instance state courts' jurisdiction given the importance and specificity of the requirements and legal norms underlying thereof."

Comments

The Appeals Court appears to have agreed that the 2009 contract was not governed by the 2015 Amendment. This was by reference to Article 438 of the Civil Code, which stipulates:

1. *A contract must comply with rules that are mandatory for the parties by virtue of a statute or other legal acts (imperative norms) in effect at the time of its conclusion.*
2. *If after the conclusion of a contract a statute is adopted establishing rules mandatory for the parties other than those that were in effect upon conclusion of the contract, the terms of the concluded contract shall remain in force except in cases when it was established in the statute that its effect extends to relations arising from previously concluded contracts.*

Two observations should be made in this regard:

First, the parties' arbitration agreement was broad and even contained the language "excluding jurisdiction of general courts," which confirms the parties' intention to avail the tribunal of unrestricted powers to decide all contractual disputes between the parties. This was consistent with the then-existing practice. Notably, in the period between 10 February 2007 (the effective date of the law on commercial arbitration) and 18 July 2014 (the date of the Cassation Court Decision), arbitration agreements were drafted without a single restrictive reference to the contract invalidity issue. The restrictive interpretation of the Civil Code emerged only as a result of the unusual Cassation Court Decision. The Appeals Court, however, concluded that in 2009, the Civil Code included mandatory rules limiting the power of arbitral tribunals to hear the contract invalidity issue. Thus, the Court found that the law prevails over the contract.

Second, by applying Article 438, the Court tacitly modified the arbitration agreement to exclude the contract invalidity issue from its scope but failed to determine the validity of the arbitration agreement as to other matters.

With regard to the claimant's second point that the 2015 Amendment targeted a specific group of disputes, as someone who personally took part in the discussions of the 2015 Amendment, I should note that, although as part of the 2015 Amendment the Parliament authorized arbitration for certain

types of post-dispute family, employment and consumer arbitrations, it is inaccurate to assert that the Civil Code was amended in the context of these disputes only. Rather, the government's policy justification (as referred to above) makes clear that the reason for the 2015 Amendment was the Cassation Court Decision.

Also, it is difficult to speculate whether the Civil Appeals Court in fact gave weight to the independence issue in this case as the Cassation Court did, but the facts that raise concerns over the independence of the arbitral institution are overwhelming. Particularly, the parties' arbitration agreement envisaged an arbitration with a panel of three arbitrators at the Arbitration Institution at the Chamber of Commerce and Industry of Armenia ("CCIA Arbitration Institution") under its rules.

The CCIA Arbitration Institution is perhaps the most commonly used arbitration institution in Armenia. According to the CCIA Arbitration Institution rules, "[b]y agreeing to arbitration to be administered by" the CCIA Arbitration Institution, "the parties have accepted that [the arbitral tribunal] shall be formed *exclusively from the list of arbitrators of the Arbitral Institution.*" The lawyer for the party that sought to uphold the arbitration clause was a partner of a law firm whose managing partner is the President of CCIA Arbitration Institution, who has broad powers under the CCIA Arbitration Institution rules and its charter, ranging from arbitrator appointments to deciding on arbitrator challenges. The lawyer himself is listed as an arbitrator on the CCIA Arbitration Institution's roster, along with five other members of the firm. The Secretary of the CCIA Arbitration Institution is also a partner of the same law firm. Further, the firm's website makes plain that the party it represented in this case is a "major client."

In such circumstances, it is unsurprising that the claimant chose to avoid the CCIA Arbitration Institution. Similarly, it is also apparent why in such cases Armenian courts have sought to ensure the integrity of the protection of civil rights through Armenia's court system.

It is hoped that Armenian litigants will genuinely realize the independent and impartial nature of arbitration. That would likely lead to a relaxation of the courts' protectionist approach and over-reaction toward arbitration, which, as evidenced in the above two cases, *may often be justified*. Ultimately, the largest burden to make arbitration more acceptable to the Armenian business community lies with the arbitration institutions, which should develop their rules and arbitration panels in accordance with the highest standards of independence and impartiality.

Finally, it is difficult to predict how the Armenian courts will apply the jurisprudence concerning contract invalidity to arbitrations between foreign parties and Armenian counterparts with a seat in Armenia. However, with regard to the enforcement of foreign arbitral awards that touch upon the contract invalidity issue, it should be noted that the Armenian Constitution stipulates that "[i]n case there is a contradiction between the norms of international treaties ratified by the Republic of Armenia and the norms of laws, the norms of the international treaties shall be applied." To that end, it is hoped that the pro-enforcement bias of the New York Convention, which Armenia ratified in 1997, will prevail, and that the Armenian courts will honour foreign arbitral tribunals' decisions concerning contract invalidity.

To make sure you do not miss out on regular updates from the Kluwer Arbitration Blog, please subscribe here. To submit a proposal for a blog post, please consult our Editorial Guidelines.

This entry was posted on Tuesday, November 19th, 2019 at 10:00 am and is filed under Arbitrability, Armenia, Central Asia, Jurisdiction of the arbitral tribunal
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.