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Arbitration And Insolvency: An Overview From Latin America

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One of the many consequences of the Covid-19 pandemic and the world-wide economic crisis has been the sharp increase of insolvency filings before national courts. Latin America is no stranger to this situation, having been part of the surge in business insolvencies. Brazil, in particular, has been a recent insolvency hotspot within Latin America.

This rise in insolvency proceedings certainly poses a challenge for those parties facing an arbitration against a company undergoing insolvency and those parties contemplating commencing an arbitration against such an insolvent entity. Not only do a number of tensions exist between insolvency proceedings and arbitration – arbitrations are often conducted behind closed doors (the private process being a product of the underlying principle of party autonomy), whilst insolvency proceedings are public with the disposal of a debtors assets being centralised in national courts (a product of the underlying principle of the equality of creditors) – but also the effects of insolvency on existing ("pending") or potential arbitration proceedings pose a number of further practical issues that parties and arbitrators will need to grapple with.

This blog post offers an overview of the interplay between arbitration and insolvency from a Latin American perspective, describing the approach that a number Latin American jurisdictions have taken – including, in particular, the effects of insolvency on commencing and continuing pending proceedings, as well as the effect on the last stage of the process, *i.e.* enforcement.

When Harry Met Sally… or when arbitration meets insolvency

Whenever arbitration meets insolvency, the parties as well as the arbitrators will likely have a long list of practical concerns about the effects of the insolvency on the arbitral proceedings. Some of these concerns have been discussed in a very recent post, including: the effect of insolvency on the validity of the arbitration agreement, the nature of the claims which can still be heard in arbitration, the continuation and conduct of the arbitration proceedings, and the effect on the enforcement of the award. The answers to these key concerns are to be found in the law applicable to each of these particular issues. This applicable law might happen to be from a Latin American jurisdiction, because a Latin American jurisdiction is either the seat of arbitration, the place where the insolvent debtor is located, where the insolvency proceedings are taking place, the location of the assets, or as the result of some other relevant connection.

As it will become clear, the approach of various Latin American jurisdictions as to the effects of

insolvency on arbitral proceedings is generally quite consistent: the insolvency proceedings of one of the parties do not always prevent the continuation of an existing arbitration. This being said, a number of important nuances should, however, be appreciated.

Latin America at a glance

A number of Latin American jurisdictions regulate the effect of insolvency proceedings on arbitration expressly in their insolvency laws. Argentina (Law 24,522 of 1995), Uruguay (Law 18,387 of 2008), and Chile (Law 20,720 of 2014) adopt this approach. Other jurisdictions – notably Brazil and Columbia – do not expressly lay out this impact. In this scenario, other insolvency provisions and the interpretation of the law by the courts on a case by case by case basis can assist in determining the effects of insolvency on arbitration.

When analysing the applicable provisions in these jurisdictions, it is important to consider that some of them carefully distinguish the impact that insolvency may have on arbitration in two scenarios: bankruptcy or liquidation (seeking to liquidate the debtor's assets) and restructuring or reorganization (seeking the rehabilitation of the debtor). At the same time, the insolvency laws also make a temporal distinction – the effects of the insolvency on the arbitration can depend on whether insolvency pre-dates arbitration or vice-versa.

The fine print of the insolvency laws

Argentina, Chile and Uruguay

Turning to the first of the jurisdictions analyzed, Article 134 of the Argentinean insolvency law establishes that the declaration of bankruptcy has the effect of turning the arbitration clauses "inapplicable", unless the arbitral tribunal has been already appointed before such declaration. In other words, arbitration is not permitted in a bankruptcy scenario, unless the arbitrators were appointed before the bankruptcy declaration was issued. The provision in Article 134 of the Argentinean insolvency law is not replicated in the case of reorganization proceedings. In this context, arbitration clauses are enforceable.

Chilean insolvency law contains a similar solution in Article in 143, stating that the centralization of claims against the debtor before the insolvency courts does not apply in pending arbitrations ("*lawsuits…that to date are being heard by arbitrators*"), or matters that are subject to mandatory arbitration by law. The rule only applies to bankruptcy proceedings – reorganization proceedings do not prevent the commencement or continuation of arbitration.

Insolvency law in Uruguay clearly distinguishes "new lawsuits" from "pending proceedings" against the debtor in two different provisions. Article 56 provides that once reorganization has been declared, *"the creditors holding a credit dated prior to such declaration"* shall not bring an arbitral claim against the debtor; otherwise the proceedings will be considered void. The situation is different for arbitrations commenced before the reorganization declaration. Article 57 establishes that ongoing arbitration proceedings pending at the time of the reorganization declaration will continue.

Brazil and Colombia

As already mentioned, Brazil does not have an express provision dealing with insolvency *vis-à-vis* arbitration. However, other provisions of Brazilian insolvency law (Law 11,101 of 2005) could be resorted to in order to determine such effect. Article 6(1) of the Brazilian insolvency law establishes that lawsuits against debtor seeking an *illiquid* amount will continue before its original forum. Given that in most of arbitration proceedings the amount claimed will be "illiquid" until there is an award, they may continue or be initiated after the insolvency declaration. Indeed, the courts have recognized the validity of arbitration agreements notwithstanding the insolvency declaration (for instance, see Interclínicas Planos de Saúde S.A. v. Saúde ABC Serviços Médicos Hospitalares Ltda, Superior Tribunal de Justiça, Medida Cautelar n. 14.295. J. 09.06.2008).

Like Brazil, Colombia also does not have express provisions governing the impact of insolvency on arbitrations. By considering other provisions of Colombian insolvency law (Law 1,116 of 2006), it appears that insolvency proceedings do not prevent arbitrations commencing or continuing. In effect, Articles 20 and 50.2 provide that the insolvency court has the exclusive jurisdiction to hear all lawsuits involving enforcement or other similar process against the debtor. Thus, given that arbitration proceedings seek the declaration of rights in an award rather than enforcement of such rights, arbitration may remain intact.

Award-holders will ultimately surrender to the insolvency

A comparative analysis of the above jurisdictions reveals that attempts to execute the award against the debtor outside of the insolvency proceedings are not permitted. Instead, award-holders are required to submit the award (along with prior recognition under the New York Convention where the award is issued outside the relevant jurisdiction) as proof of their credit before the insolvency court in order to be paid from the debtor's assets and according to the relevant insolvency laws. This is the case, for instance, in the insolvency laws of Argentina (Article 56), Uruguay (Article 59), Chile (Article 135), Colombia (Article 20), and Brazil (Article 6). This certainly accords with the *par condition creditorum* principle (equal treatment of creditors), an underlying principle of all the insolvency regimes analyzed.

Conclusion

Whilst the sample of jurisdictions considered in this article should not be taken as an exhaustive analysis of the approach of Latin American jurisdictions to the interplay between arbitration and insolvency, it is nonetheless useful in helping us to reach some preliminary conclusions on the tension between these two regimes in the region.

Broadly speaking, arbitration seems to prevail over insolvency when arbitral proceedings are commenced before the declaration of insolvency. This is more evident when the debtor only faces reorganization or restructuring proceedings rather than bankruptcy given that, among other differences, the debtor still retains the administration of its assets. Despite this "permissive" regime, however, award creditors will still have to appear before an insolvency court in order to

enforce the award, and wait to be paid along with other creditors, who may have priority under the relevant insolvency laws.

In any event, it is clear that it is preferable for there to be express legislative provisions in place which deal with the interplay between the arbitration and insolvency regimes. Legislation of this kind is the best way to provide predictability to the parties (and also to arbitrators) involved in arbitral proceedings where one party is insolvent.

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