Kluwer Arbitration Blog

Surprising News From Georgia: Court of Appeals Finds Arbitral Tribunals Lacking Competence Despite a Valid Arbitration Agreement

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Despite many years of hard and tireless work for the purposes of ADR promotion in Georgia, the recent attitude of the courts towards arbitration causes significant problems at the level of basic concepts and principles. To demonstrate this, it is enough to take a look at two high-profile 2023 decisions of the Tbilisi Court of Appeals ("CoA" or "the court").

Alleged "Impartiality" as a Ground for Denial of Tribunal Competence

First, the judgment of 11 May 2023 (case N 2b/1605-23) addressed the issue of the competence of the arbitral tribunal. In particular, the applicant applied to the CoA with the request to declare that the tribunal is without competence to decide the issue posed to it. The applicant alleged that the legal representative of the claimant in the arbitration procedure was at the same time listed as the arbitrator (not serving in the capacity of an arbitrator in the present dispute) at the same arbitration center that was administering the dispute at hand. The applicant that argued that the tribunal could not have been objective in deciding the dispute.

According to the opposing party, the CoA was not authorized to recognize the party's claim as admissible until the tribunal determined the issue by itself. At the same time, the party noted that the arbitration center, where the legal representative of the party is referred to as an arbitrator, was only administering the dispute, and the dispute itself would be reviewed by a person/arbitrator chosen by the parties.

The court shared the applicant's position. It pointed out that the parties' agreement on a particular arbitral institution was not at dispute and drew attention to the fact that, since the applicant disputed the competence of the tribunal on the basis of the standard of impartiality, it was incorrect to apply the rule established by the first paragraph of Article 16 of the Law of Georgia on Arbitration ("Law") according to which the arbitral tribunal would determine its own competence. The court explained that in the case when the arbitration agreement is disputed, the party had to apply to the tribunal in order to determine its competence. However, in the given case, according to the court, the applicant questioned not the validity of the arbitration agreement, but "the objectivity of the proceeding to be determined by the tribunal". The court noted that the factual circumstances (presence of a party's representative on the list of arbitrators at the center) cumulatively created a

reasonable doubt and probability of potential influence in the decision-making process, since there was a conflict of interest in the arbitration proceedings.

If, in the present case, the applicant disputed the competence of the tribunal on the basis of partiality and not the validity of the arbitration agreement, the question arises as to why the tribunal could not determine this issue itself in the context of Article 16 of the Law? The first paragraph of Article 16 empowers the tribunal to make determination on its own competence, including (but not limited to) the determination of the existence or validity of the arbitration agreement. Under the Law, the arbitral tribunal has a broader right to determine competence rather than only in the cases when a party is challenging the validity of the arbitration agreement. Moreover, Article 9.1 of the Law obliges the court to terminate the proceedings and refer the parties to arbitration unless it finds that the agreement is void, invalid or incapable of being performed. The validity of arbitration agreement was not disputed by the applicant in the present case and has been confirmed through the judgment of the court.

At first glance, the judgment on competence is a narrow legal problem. However, a similar development of judicial practice can have wide and problematic consequences. In this particular case, the judgment lacks clarity in the context of Article 356[1] of the Civil Procedure Code of Georgia ("Code"). It also provides ambiguous reasoning of the court while determining the objectivity of the proceedings. It is unclear as to why the court decided that its intervention did not go beyond the legal framework established by Article 6, Clause 2 of the Law which states that any kind of intervention by a court into legal relations that are governed by this Law is impermissible, except where so provided for in this Law.

Alleged "Impartiality" as a Ground for Cancellation of Interim Decision on Competence

The second judgment (case N2b/3653-23) is dated 4 September 2023. Here, the applicant appealed to the Court of Appeal, challenging the tribunal decision of 29 May 2023 that had confirmed the latter's competence. The applicant pointed out that the official representative of the party in the arbitration dispute was, at the same time, an arbitrator at the center administering the dispute and due to the aforementioned circumstances, the applicant in the arbitration proceedings was restricted from the right to "equal treatment" provided by Article 3 of the Law.

Here, the CoA was asked to decide whether the arbitral tribunal was competent to consider the dispute, and subsequently whether it was in a position to rule regarding the material circumstances of the case. The existence of a valid arbitration agreement was not brought into question by the applicant.

In its reasoning, the court pointed out that the prerequisite for the successful completion of a case through arbitral proceedings required independent and impartial decision-making. The court drew attention to the fact that the legal representative of the opposing party simultaneously "worked" at the arbitration center (to be more precise, as in the previously discussed case, the legal representative of the party was listed as an arbitrator). The court noted that the said circumstance created a reasonable doubt and the likely assumption that the tribunal selected for the purposes of resolving the dispute could have been influenced at the time by the opposing party's legal representative who "worked" at the same arbitration center.

Relying on the circumstances above, as the grounds for justifying the partiality of the tribunal, the court ignored the requirements of Article 16.5 of the Law as well as Article 356[16] of the Code as per which the court's ruling on the competence of tribunals must be substantiated. The court's reasoning required proper clarification; i.e., a clear indication of the facts and reference to legitimate grounds in relation to the particular case. The simple fact of the legal representative "working" at the arbitration center as a cause for justification is far from satisfying the legislative threshold and should not have constituted the grounds for making a substantiated assumption regarding the partiality of the tribunal – the same tribunal which was at the same time appointed by the parties of the dispute.

Conclusion

According to the Article 356[13] Paragraph 3 of the Code, matters related to the competence of the arbitral tribunal shall be heard by courts of appeal. According to the Article 356[16] Paragraph 3 of the Code, a court ruling on the competence of the arbitral tribunal shall be final and may not be appealed. Given the fact that the aforementioned judgments cannot be appealed, they call into question the existence of arbitration as a viable alternative to litigation in Georgia. They undermine Georgia's status as a state that supports and encourages arbitration as alternative mechanism of dispute resolution.

These judgments are a signal to the Georgian courts that they can, regardless of the existence of a valid arbitration clause, intervene in the arbitral proceedings, including setting aside the tribunals' determination on its own competence without providing a legally sound justification.

Moreover, the judgments call into question the generally recognized competence-competence doctrine (which is recognized by the Law), undermine the principle of non-interference in the arbitration process, restrict lawyers from acting as arbitrators, and open the door to future unjustified and ill-considered decisions.

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