Is C-700/20 a new manifestation of the ECJ's "arbitration unfriendly" approach?

Court decision leads to significant implications for commercial arbitration

26 January 2023

As the new year starts, it is always a great time to look back at happenings of the past 12 months. We have looked at developments in the arbitration field over the past year.

2022 proved to be another exciting year for arbitration. One decision in particular caused a major stir, which brought about a significant change in the field and raised a number of questions about the "acceptance" and perception of arbitration by the **Court of Justice of the European Union** (hereinafter: "ECJ").

The astonishing decision in case *C-700/20* of the ECJ has completely rocked the arbitration boat and had a severe impact on the relationship between commercial arbitration and court proceedings in the EU.

> The practical effect of this ECJ decision is that **Member States have to ignore the existence of recognised foreign arbitral awards, where the award was rendered contrary to the (recast) Brussels I Regulation's provisions** (which does not otherwise apply to arbitration) **when the recognition of a later judgment of a Member States' court on the same subject matter is sought**.

Let's dive into the details of the decision!

1. Introduction

One of the fundamental objectives of international arbitration is to provide a final, binding resolution of the parties' dispute. Article III of the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (hereinafter: "New York Convention") states that:

> *"Each Contracting State shall recognise arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the award is relied upon, under the conditions laid down in the following articles [particularly Article V]."*

As pointed out by many scholars, the New York Convention does not expressly address the preclusive nature of an arbitral award. However, Article III of the New York Convention forms an obligation on the Contracting States to recognise the awards, which is not just a formal act but also a recognition that makes an award binding. Thus, we can go further with the conclusion that Article III of the New York Convention does concern the preclusive effect of

an arbitral award by providing a basic principle to be followed and also elaborated upon by the courts and arbitral tribunals.[1]

In connection with the decision of the ECJ in case C-700/20[2], one key question arises: whether the ECJ's decision fits in line with the existing pattern that many scholars consider as "unfriendly" towards arbitration. The main finding of the ECJ was that **a judgement adopted by a court of a Member State in the terms of an arbitral award can in principle be the basis for a refusal to recognise a later irreconcilable judgment of another Member State.** However, this rule does not apply when the recognition judgment results in an outcome that a Member State court could not have reached directly without infringing the provisions and the fundamental objectives of the Brussels I Regulation.

2. Background of the case

The background of the ECJ's decision in case C-700/20 goes back until 2002, when an oil tanker called "Prestige" sank off the coasts of Galicia, Spain. The tanker was transporting 70,000 tons of oil which subsequently spilled into the ocean. This caused an oil spill disaster and resulted in significant damage to the coastal areas of Spain and France. By the end of 2002, the Spanish State referred the case to a Spanish Court in the form of criminal proceedings against the captain and the owners of the ship Prestige and also started proceedings against the London P&I Club, the liability insurer of both the vessel and its owners. However, the insurance contract concluded between the owners of the ship and the London P&I Club contained an arbitration clause. The arbitration clause stipulated that in the case of a dispute, the seat of the arbitration would be London, United Kingdom.

The London P&I Club did not appear at the trials before the Spanish Court. However, in 2012 arbitration proceedings commenced in London seeking a declaration that Spain was permitted to pursue its claims in those arbitration proceedings based on the arbitration clause in the insurance contract. The Arbitral Tribunal published an award on 13 February 2013 in which it held that as the Spanish governments' claims were contractual in nature, with the application of the English conflict of laws principles, the law to be applied to the contract was English Law.

Arbitration in England is governed by the Arbitration Act of 1996, which states under Section 66(1):

> *"An award made by the tribunal pursuant to an arbitration agreement may, by leave of the court, be enforced in the same manner as a judgment or order of the court to the same effect."*[3]

In England, an arbitration award could be enforced if permission (leave) was obtained by the Court. The requirement for obtaining leave is to make a request to the court. Therefore, after the publication of the award, the London P&I Club applied to the High Court of Justice and the Queen's Bench Division under Section 66(1) and (2) of the Arbitration Act to enforce the arbitral award in that jurisdiction in the same manner as a judgment or order and for a judgement to be entered in the terms of that award. Such a "recognition judgement" was made by the Court in October of 2013.

The already complicated situation became even worse, when the parallel proceedings in Spain ended, as the Spanish Court held London P&I Club liable for the civil claims to the contractual limit of liability of USD 1 billion. The Spanish Court made an enforcement order in March 2019 in which it determined the amounts that each of the claimants were entitled to obtain from the respondents. In 2019, Spain made an application to the High Court of

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[1] 'Chapter 27: Preclusion, *Lis Pendens* and *Stare Decisis* in International Arbitration', in Gary B. Born , International Commercial Arbitration (Third Edition), 3rd edition (© Kluwer Law International; Kluwer Law International 2021) pp. 4099 - 4204

[2] https://curia.europa.eu/juris/liste.jsf?num=C-700/20

[3] https://www.legislation.gov.uk/ukpga/1996/23/section/66/enacted

Justice (England & Wales), Queen's Bench Division (United Kingdom) in order to ensure the recognition of the enforcement order in the United Kingdom. The application was made on the basis of Article 33 of Brussels 1 Regulation, pursuant to which, a Member State must recognise a judgment from another Member State without any special procedure being required.

One key issue needs to be highlighted before dealing with the actual decision of the ECJ: the doctrine of "*lis pendens*" in international arbitration.[4] The "*lis pendens*" or "lawsuit pending" is addressed by Article 27 of the Brussels 1 Regulation, which however, does not include arbitration in its scope. The main aim of *lis pendens* is to achieve procedural order and efficiency, and to protect the parties from an adversary commencing multiple proceedings based on the same claim against the same respondent. The latter would result in an unjust situation. As Born points out, the application of the *lis pendens* doctrine is largely based on *sui generis*; however, the premises of the doctrine do not necessarily apply in the context of international arbitration.[5] Arbitration is a kind of privatised jurisdiction, where the parties declare based on their private autonomy that they want to derogate from the judicial system of the state and therefore, take the adjudication of their existing or future legal dispute out of the enforcement and dispute resolution paradigm defined by the state. With such an agreement, only one competent forum, namely the arbitration forum itself could exist. **Thus, if there is a national court judgment that breaches the arbitration agreement of the parties, it should not have preclusive effect in the arbitration. Therefore, a stay or suspension of arbitral proceedings remains a tool that could be used only in extraordinary cases.[6]**

Turning back to the relevant proceedings of the case, the High Court of Justice (England & Wales), Queen's Bench Division (United Kingdom) granted Spain's 2019 application by order. The London P&I Club lodged an appeal against the order to the referring court (High Court of Justice Business and Property Courts of England and Wales), claiming that the enforcement order is irreconcilable within the meaning of Article 34(3) of Brussels 1 Regulation with the order and judgment of the Tribunal that was confirmed by the Court of Appeal (England & Wales) (Civil Division) in 2015. In their appeal, the London P&I Club also referred to the enforcement of the order to be contrary to public policy as regarding inter alia the principle of *res judicata*.

Thus, the referring court turned to the ECJ for a preliminary ruling with three questions:

a) whether a judgement given under Section 66 of the Arbitration Act qualifies as a judgment within the meaning of Article 34(3) of Brussels 1 Regulation;

b) whether a judgment that in line with Article 1(2)(d) of Brussels 1 Regulation falls outside the material scope of the regulation, could still be relied on to prevent recognition and enforcement of a judgment from another Member State pursuant to Article 34(3);

c) assuming that Article 34(3) does not apply, whether 34(1) could be a ground for refusing recognition or enforcement of a judgment from another Member State on the basis that such recognition or enforcement would disregard the force of *res judicata* acquired by a domestic arbitral award or a judgment entered in the terms of such an award.

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[4] *Lis pendens*, literally meaning "a suit pending," is a related doctrine aimed to prevent two judicial bodies dealing with the same dispute at the same time. *Lis pendens* therefore prevents the initiation of new proceedings on a matter if there is already an existing case pending before a court or tribunal. In: Norah Gallagher, 'Chapter 17: Parallel Proceedings, *Res Judicata* and *Lis Pendens*: Problems and Possible Solutions', in Loukas A. Mistelis and Julian D.M. Lew (eds), Pervasive Problems in International Arbitration, International Arbitration Law Library, Volume 15 (© Kluwer Law International; Kluwer Law International 2006) pp. 329 – 356

[5] 'Chapter 27: Preclusion, *Lis Pendens* and *Stare Decisis* in International Arbitration', in Gary B. Born , International Commercial Arbitration (Third Edition), 3rd edition (© Kluwer Law International; Kluwer Law International 2021) pp. 4099 - 4204

[6] 'Chapter 27: Preclusion, *Lis Pendens* and *Stare Decisis* in International Arbitration', in Gary B. Born , International Commercial Arbitration (Third Edition), 3rd edition (© Kluwer Law International; Kluwer Law International 2021) pp. 4099 - 4204

3. Decision of the ECJ

In its decision, the ECJ concluded that arbitration falls under the general exclusion rule of Brussels 1 Regulation embodied in Article 1(2)(d); however, that does not preclude a judgment relating to an excluded matter from coming within the scope of Article 34(3). Therefore, a judgment in the form of an arbitral award made in a Member State could prevent the recognition and enforcement of a judgment given by another Member State, if they are irreconcilable. However, the ECJ held that this rule does not apply in the present case. The provisions of EU law shall not only be interpreted by the wording, but also context of it and the purpose of the legislation. Therefore, the ECJ held that the previously mentioned rule could not be applied where the recognition judgment leads to a result which could not have reached by a national court of a Member State without infringing the provisions and fundamental objectives of the Brussels 1 Regulation. The main purpose of the Regulation inter alia is to provide mutual trust in the administration of justice in the EU and to strengthen judicial cooperation.

According to the ECJ, the arbitral award infringed two fundamental rules of the Brussels I Regulation. First, this occurred by relative effect of the arbitration agreement in an insurance contract. As elaborated in case law, the jurisdiction clause agreed between the insurer and the insured party cannot be invoked against a victim of an insured damage who wishes to bring a claim directly against the insurer before the courts for the place where the harmful event occurred (or its domicile).

The second problem with the circumstances of the case was connected to *lis pendens*. On the date when the arbitral proceedings were commenced, the proceedings were already pending between the Parties before the Spanish Court. As all of the conditions of Article 27 prevailed in the present case (same parties, same cause of action, courts of different Member States), the circumstances amount to a situation of *lis pendens*; therefore, any court other than the court first seized must of its own motion stay its proceedings until such time as the jurisdiction of the court first seized has been established, and then, where the jurisdiction of the court first seized is established, decline jurisdiction in favour of that court.

The decision established the following. **The judgment entered by a court of a Member State in the terms of an arbitral award does not constitute a 'judgment' within the meaning of Article 34(3) of Brussels I Regulation, where a judicial decision resulting in an outcome equivalent to the outcome of that award could not have been adopted by a court of that Member State without infringing the provisions and the fundamental objectives of that regulation, in particular as regards the relative effect of an arbitration clause included in an insurance contract and the rules on lis pendens contained in Article 27 of that regulation.**

Therefore, with these circumstances prevailing, Article 34(3) must not be interpreted as meaning that a judgment entered in the terms of an arbitral award can prevent the recognition of a judgment from another Member State.

The third issue concerned whether in the absence of Article 34(3), Article 34(1) could form a ground to refuse the recognition and enforcement of a judgment from another Member State, **as it would be contrary to public policy of that State, as it disregards the force of *res judicata* acquired by the judgment**. According to the ECJ, the answer is no. As the judgment entered in the terms of an arbitral award was made in such circumstances that did not comply with the purpose of the Regulation (ignoring the relative effect of an arbitration agreement and *lis pendens*), the infringement of public policy could not be established either. As it was pointed out by the ECJ, the case law concerning public policy could be referred to only in extraordinary cases.

4. Assessment of the decision

The significance of the case stems from the fact that it concerns competition between national judicial systems and arbitration, as has been noted by scholars. The ECJ had to decide on questions such as the buffer points between

the *res judicata* effect of an arbitral award and the judgment of a national court. Furthermore, the issue of *lis pendens* was addressed as well, which also has great significance, as the doctrine is not readily applied in international arbitration. There are currently a number of outstanding issues triggered by this controversial ECJ decision.

An important aspect of the case arises from the fact that the ECJ issued findings in relation to arbitration not covered by the scope of the (recast) Brussels 1 Regulation for the infringement of the provisions and the fundamental objectives of the (recast) Brussels I Regulation. In this context, the decision could lead to the interpretation that arbitrators should take into account the "provisions and the fundamental objective" of the (recast) Brussels I Regulation to ensure the full recognition of their award in a Member State. It practically means that **the ECJ (indirectly) subjected arbitral tribunals to the provisions of the (recast) Brussel I Regulation through the backdoor of recognition.** This is a problem in itself, but a further issue is whether a Regulation, the scope of which does not cover arbitration, should be taken into account by arbitrators at all, and if so, what scope should be considered, since the decision has defined it very broadly with the expression of "the provisions and the fundamental objective". Consequently, **this decision of the ECJ may encourage parties to avoid the use of arbitration agreements**.

This is in itself decisive as to whether this decision can fit into the "arbitration-unfriendly" attitude of the ECJ (see the following cases: West Tankers (C-185/07), Achmea (C-284/16), Komstroy (C-741/19)). A particularly interesting aspect of this decision is that the ECJ's prior arbitration unfriendly attitude has been demonstrated in the area of investment arbitration, as these cases show. Case C-700/20, however, struck a blow in the field of commercial arbitration.

Further to this, the decision may also encourage arbitrators to use the institution of stay of the proceedings. However, it is a fundamentally alien institution to arbitration. In addition, the one-way application of the *lis pendens* doctrine raises problems as well, which is also evident from the decision.

In fact, only one thing is certain, that these issues will be the subject of intense debate in the years to come.

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