Enforcement of International Arbitral Awards in Russia—Still a Mixed Picture

By Boris Karabelnikov and Dominic Pellew***

Introduction

Russian companies play an increasingly important role in the world economy, both as suppliers of commodities and as owners of assets abroad. At the same time, foreign direct investment into Russia is increasing, with significant attention now being paid, for example, to opportunities in the power generation and transportation sectors. The need for reliable dispute resolution mechanisms in contracts involving Russian parties has never been more acute.

Court litigation remains, in most cases, an undesirable option: the Russian courts are seen as inefficient at best, and judgments from outside Russia are not enforceable in Russia in the absence of a specific treaty with the country in question.[1] Arbitration, it might be thought, is the only viable alternative. After all, Russia has an up-to-date and sophisticated law on international commercial arbitration (based on the UNCITRAL Model Law on International Commercial Arbitration), and since 1960 has been a party to the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention). But how is the law applied in practice? In particular, how enforceable are international arbitral awards in Russia?

Articles on this subject have been written in the past, and their conclusions are generally pessimistic.[2] There are two particular reasons for re-addressing the subject now. Firstly, the enforcement of arbitral awards received the particular attention of the Supreme *Arbitrazh* Court (SAC)—Russia's highest commercial court—at the beginning of 2006, when it published an 'overview' of judicial practice relating to the enforcement and challenge of arbitral awards. Such overviews are intended as a guide for the lower courts. Two years have passed since the overview was published and it is now possible to take stock of how that guidance has, or has not, been followed. Secondly, 2008 is both the 50th anniversary of the 1958 New York Convention and a year in which a new Russian President has been elected. A general assessment of Russia's attitude to foreign investment as well as its implementation of the Convention in particular is therefore timely.

* Arbitrator, International Commercial Arbitration Court at the Chamber of Commerce and Industry of the Russian Federation; Professor of Law, Moscow School of Social and Economic Sciences; member, London Court of International Arbitration; bkarabelnikov@hotmail.com
** Partner, Lovells CIS, Moscow; dominic.pellew@lovells.com

1 Russia has signed very few such treaties with countries outside the former Soviet Union. In Europe the only such countries are Greece, Italy, Spain and Cyprus.

2 See e.g. H. Oda, 'Enforcement of International Commercial Arbitration Awards in Russia' (2005) 16:2 ICC ICArb. Bull. 51; V. Khvalei & J. Benedictsson, 'Recognition and Enforcement of Foreign Arbitral Awards in the Russian Federation' [2005:1] Stockholm Int. Arb. Rev. 23; G. Babitchev, 'Le contrôle judiciaire des sentences internationales dans la Fédération de Russie', Rev. arb. 2002.71.

This article focuses primarily on enforcement of international awards in Russia (i.e. both foreign awards and international awards issued in Russia). Clearly, challenges to awards are also relevant to an analysis of attitudes of Russian courts towards arbitration. However, Russian case law relating to challenges tends to present a more positive picture than that relating to enforcement, in part because challenges are almost always heard by courts in the Moscow Region (as Moscow is normally the seat of the arbitration). Enforcement proceedings, on the other hand, are heard by courts at the place where a company is registered or has assets, which will often be outside Moscow, particularly in the case of natural resource exporters. Because of their role in challenge proceedings, Moscow courts have accumulated more experience of dealing with cases relating to international commercial arbitration than other regional courts and are generally more sophisticated in their approach. Yet, successful defences to challenges do not necessarily translate into successful claims for enforcement, especially where the latter are heard before different regional courts.[3] Furthermore, given the preference shown by contracting parties for non-Russian institutions and/or non-Russian seats in high value contracts, awards issued in Russia tend to be smaller in financial terms than foreign awards. The main area of interest for a foreign investor is therefore enforcement of foreign awards under the New York Convention.

Although this article does not claim to provide a comprehensive analysis of all possible complications faced by claimants seeking to enforce awards in Russia, it sets out (I) a summary of recent Russian judicial practice, including an analysis of some of the most common legal problems encountered by investors at the enforcement stage; (II) a history of the most important individual cases involving foreign investors decided by Russian courts over the past two years; and (III) some practical tips for claimants on how to maximize their chances of success in the Russian courts.

I. Recent Russian judicial practice concerning matters involving international arbitration

A. Legal framework

Russia's national law on international commercial arbitration dates from 1993 and, as mentioned above, closely follows the UNCITRAL Model Law on International Commercial Arbitration. Russia is also a party to both the New York Convention and the 1961 European Convention on International Commercial Arbitration. In practice, however, Russian judges have had brief experience of applying such legislation, since disputes involving international arbitration agreements only began to appear in the Russian courts after the break-up of the Soviet Union in the early 1990s. Furthermore, jurisdiction over claims for enforcement of international arbitration awards used to be shared between the *Arbitrazh* courts[4] and the courts of general jurisdiction. On 1 September 2002, however, jurisdiction over such claims was given exclusively to the

3
One recent decision of the federal *Arbitrazh* court in the Moscow Region suggested that a successful defence to a challenge in Russia would have *res judicata* effect with respect to a subsequent enforcement proceeding in Russia (*Montana Invest* v. *Realinvest*, 27 March 2006 , KG-A40/ 2138-06,). Whether this truly represents the state of Russian law is, however, doubtful.

4
Arbitrazh courts are State courts, used for the resolution of commercial disputes. They should not be confused with arbitral tribunals. The expression '*Arbitrazh* court' is sometimes translated by other authors as 'commercial court'.

Arbitrazh courts, with the result that some of the courts within that system lacked experience in applying the relevant laws and principles governing international arbitration. As mentioned above, this applies less to courts in the Moscow Region, given their experience of challenge proceedings, and perhaps those in the North-Western Region covering St Petersburg.

Proceedings for the enforcement of arbitral awards involve three—or, more precisely, two and a half—instances in the Russian court system. The first court to which a foreign claimant must turn is the *Arbitrazh* court at the place where the defendant (or its assets) are located. The decision rendered by that court is not open to appeal, in the sense of a full review of the merits,[5] but a party can refer the decision to a higher *Arbitrazh* court at cassation level. The cassation court reviews the first decision and can quash it for any evident error of law or procedure (it should be noted that cassation court hearings rarely last longer than thirty minutes). Finally, a party that is still dissatisfied after the cassation decision can make a request to the SAC for a supervisory review of the lower decision(s). The SAC decides at its own discretion whether or not to allow such review (hence the reference above to half an instance). If it does, the review is carried out by the Presidium of the SAC and a decision reached that either approves or sets aside the previous judgments. In the latter event, the Presidium will generally refer the case back to the first instance court for a new decision. Exceptionally, however, it may issue a final and binding decision without referring the case back.

Although there is no notion of binding precedent in the Russian legal system, the decisions of the SAC Presidium are carefully examined by Russian lawyers and often point to trends being taken in the judicial system with respect to certain types of cases. The SAC can also clarify court practice with regard to various types of cases by way of plenary resolutions or the overviews referred to in the introduction above.

In early 2006, the SAC published such an overview in the form of Informational Letter No. 96, dated 22 December 2005, relating to recognition and enforcement of the judgments of foreign courts and the challenge and enforcement of arbitral awards (the 'Overview'). It clarified the approach of Russian courts to certain issues relating to the enforcement of arbitration awards (such as the requirement that arbitrators should be independent). However, many uncertainties in the law are not dealt with in the Overview, which is moreover ambiguous or—in the view of the present authors—plainly wrong in certain respects (some of which are commented on below). The Overview also adopts the practice of restating the cases it cites rather than quoting them verbatim. It is therefore the restated case rather than the actual case that serves as a model. Sometimes, key facts in the original decision are left out, leaving it unclear whether the SAC is trying to 'correct' the decision in question or approve it.[6]

Each year, the SAC publishes statistics on the categories of claims heard by the *Arbitrazh* courts.[7] Statistics for 2007 indicate that the *Arbitrazh* Courts heard 1,668 cases involving foreign companies or individuals in that year (compared with 1,595 in 2006). They

---

5 Appeals do exist in other matters dealt with by the *Arbitrazh* courts. They were removed from enforcement proceedings only in 2002.

6 For a detailed analysis of the Overview see B. Karabelnikov, 'The Supreme *Arbitrazh* Court of the Russian Federation Does Not Trust International Arbitration' (2006) 72:2 *Arbitration* 130; D. Kurochkin, 'Several Commentaries to Recommendations of the Presidium of the SAC Concerning Recognition and Enforcement of International Arbitral Awards and Foreign Judgments', *Mezhdunarodny Kommerchesky Arbitrazh* 2006/3, 66 (in Russian).

7 <www.arbitr.ru>. The statistics are available only in Russian.

included 106 claims for recognition and enforcement of foreign judgments or arbitral awards.[8] No information is given on the number of awards concerned or the outcome of the actions. This is unfortunate, as not all Russian court decisions are published, so it is impossible to compile statistics from primary sources. Most decisions of the lower *Arbitrazh* courts for 2007 (and for previous years) are inaccessible to the general public. As for the higher instances (appeal and cassation), only around 50–60% of the decisions dating from the last three to five years are now publicly available. The situation improved somewhat in 2006, when all state *Arbitrazh* courts created websites, but information contained on those sites covers only the most recent cases and relevant cases cannot be found quickly without a case number. It is hoped that all cases heard by Russian courts will soon become available online, enabling commentators to prepare their own analyses without having to rely on the SAC's figures. In any event, the present authors suspect that many of the 106 (or 118) claims identified in the SAC statistics for 2007 relate to enforcement of judgments from the courts of CIS (former USSR Republic) countries, not international arbitral awards.

Through various public and private sources, the present authors have assembled material concerning some 30 different cases involving claims for enforcement of foreign arbitral awards subsequent to 1 September 2002 (i.e. when the *Arbitrazh* courts acquired exclusive jurisdiction over such claims). The word 'case' here refers to claims relating to a given award, no matter how many court judgments were necessary before a final decision was reached. Fewer than 50% of these claims were granted. Most of the judgments refusing enforcement apply questionable reasoning with respect to the New York Convention and regrettably fall far short of the pro-arbitration standards of key European jurisdictions such as France, Switzerland and Sweden. It should also be borne in mind that this analysis does not include cases where *Arbitrazh* courts have refused to give effect to arbitration clauses and instead accepted jurisdiction in breach of Articles II and III of the New York Convention, or cases where they have declared contracts containing arbitration clauses (or arbitration clauses within contracts) to be invalid.

An analysis of the 30 cases reveals the recurrent use of certain tactics by Russian defendants. The most common grounds relied upon are: (i) transfer of the burden of proving lack of proper notice of the arbitration proceedings (New York Convention, Article V.1(b)) from defendant to claimant; (ii) misuse of the public policy ground (New York Convention, Article V.2(b)); (iii) creation of a conflict between enforcement of the international arbitral award and a local court judgment in a related action involving the same subject matter; and (iv) incorrect application of the exclusive jurisdiction of state *Arbitrazh* courts to limit the range of arbitrable disputes. Each of these grounds is analysed below, together with the impact (if any) of the Overview and most recent case law.

B. Burden of proving proper notification transferred from defendant to claimant

Before publication of the Overview, Russian courts often refused to enforce international arbitral awards owing to the claimant's failure to prove that the defendant had been

---

8 Source: 'Summary of Main Indicators of the Work of the *Arbitrazh* Courts of the Russian Federation 2006–2007'. Confusingly, the SAC also quotes a figure of 118 claims for recognition and enforcement of foreign judgments or arbitral awards in 2007 in a separate document, 'Explanatory Note to the Statistical Account of the Work of the Arbitrazh Courts of the Russian Federation in 2007'. (Both documents (in Russian) are on the SAC's website referred to *supra* note 7.)

properly informed of the arbitration proceedings. Such practice was in open disregard of the terms of Article V.1(b) of the New York Convention and the equivalent provisions of the UNCITRAL Model Law, which make it quite clear that it is up to defendants to prove that they were not properly informed, not for claimants to prove the contrary. For example, on 15 December 2003 the federal *Arbitrazh* court for the Moscow Region refused enforcement of a foreign award, observing that 'the statement by [the defendant] that it had not been properly notified could have been countered if [the claimant] had provided the *Arbitrazh* court with the necessary proof. However, this was not done'.[9] Similarly, in a judgment dated 18 April 2005, the federal *Arbitrazh* court for the North Caucasus Region refused enforcement of a foreign award against a Russian party that had participated in all but the final hearing, as there was 'an absence of documents proving proper notification'.[10]

The tendency of Russian courts to require the claimant to provide positive evidence of proper notification, when the defendant claims that it has not been properly notified, might be thought of as understandable in view of the difficulty of proving a negative. However, it is clearly contrary to the wording of the New York Convention. Besides, it is not impossible for a defendant to discharge itself of this burden, even in Russia. In a case concerning the challenge of a 2003 award issued by a tribunal appointed under the rules of the International Commercial Arbitration Court at the Chamber of Commerce and Industry of the Russian Federation (MKAS[11]), a Russian defendant produced a letter from the courier company used by MKAS showing that all official communications from the tribunal had been delivered to a different company at a different address. This was accepted by the federal *Arbitrazh* court for the Moscow Region as adequate proof that proper notice had not been received.[12]

Foreign litigants surprised by the willingness of Russian courts to accept the argument that defendants have not been properly informed should be aware that it is not unknown in *Arbitrazh* court practice for written pleadings to be deliberately withheld from opponents. For example, the sending of empty envelopes (providing the sender with courier receipts to 'prove' that documents were delivered) is not unheard of. Such abuses are familiar to *Arbitrazh* court judges, which may help to explain why they are prepared to accept that similar practices may occur in international arbitration.

There appeared to be some progress in relation to the New York Convention's proper notification ground when, in February 2005, the Presidium of the SAC, in a decision overturning two lower instance decisions refusing enforcement of a Stockholm Chamber of Commerce award, insisted that the defendant must prove that it had not been properly notified. The Russian defendant had argued, among other things, that notice had been sent to its counsel and not to the company's legal address. After establishing that the counsel was fully authorized to handle the case on behalf of the defendant company, the SAC held that enforcement could not be refused on this ground and pointed out that, in accordance with the New York Convention, the burden of proving this ground lies with the party opposing enforcement.[13]

9
Federal *Arbitrazh* court for the Moscow Region, 15 December 2003, KG-A40/9235-03, *Forever Maritime* v. *Mashinoimport*. The judgment was left unchanged by the Presidium of the SAC in its judgment of 22 June 2004, no. 3253/04.

10
F08-1372/2005, *Itera Pet* v. *Kavminkurortrozliv*.

11
The Russian acronym stands for *Mezhdunarodny Kommercheskiy Arbitrazhny Sud* (International Commercial Arbitration Court). MKAS is the main Russian international arbitration institution.

12
Federal *Arbitrazh* court for the Moscow Region, 22 May 2003, KG-A40/2879-03, *Al Fatkh* v. *Worldwide Transfer*.

13
Presidium of the Supreme *Arbitrazh* Court, 22 February 2005, 14548/04, *Codest Engineering* v. *Most Group*. An English translation of the judgment may be found in [2005:1] Stockholm Int. Arb. Rev. 237.

This case was included in the Overview (at paragraph 23), which is encouraging. Sadly, however, the restated case is much less clear about the burden of proof than was the original decision. The heading summarizing the case merely states as follows: 'An *Arbitrazh* court cannot set aside an arbitral award if the party to the proceedings was properly informed of the date of the hearing and made an appearance.'

The Presidium of the SAC has since rendered two more decisions—both on 11 April 2006—in which it emphasized that 'the burden of proving the facts amounting to improper notification and the impossibility of presenting its case for other reasons lies on the party challenging the arbitral award'.[14] On 11 September 2006, however, the federal *Arbitrazh* court for the Central District refused enforcement of a foreign arbitral award, again on the ground that 'the appropriate evidence was not provided that [the arbitral tribunal] had properly informed [the defendant] about the examination of the case'.[15] Ignoring the claimant's reference to the New York Convention's provision on burden of proof, the *Arbitrazh* court found that the defendant had not been properly notified despite the fact that correspondence from the tribunal had been sent to the address on the defendant's official letterhead.

A more encouraging—albeit double-edged—precedent was recently provided by the federal *Arbitrazh* court for the Far Eastern Region. In a judgment dated 6 March 2007 the court allowed enforcement of a US award because there was decisive evidence that notice had been sent to the defendant both by fax and registered mail. It should be noted, however, that in reaching this conclusion the court notably relied only on evidence provided by the claimant, not the defendant.[16]

The last word on the proper notification ground unfortunately goes to two decisions made by the federal *Arbitrazh* court for the Moscow Region on 17 April and 15 May 2008. The court denied enforcement of two awards issued by the London Court of International Arbitration (LCIA) in London against the Russian defendant (a State-owned company), on the ground that, although the defendant had been given ample notice of the date of the hearing and the fact that it would take place in London, the hard copy document informing it of the precise venue reached it only five days before the hearing. The court held that this left the defendant's representative with insufficient time to obtain a British visa. Why it was supposedly necessary for the representative to receive a document indicating the venue in order to obtain a visa was not considered by the Court. Moreover, the defendant in actual fact never applied for the visa.[17]

The conclusion seems to be that although Russian courts are capable of correctly assigning the burden of proof in relation to proper notification, they are likely to continue, at least for the foreseeable future, to misunderstand (deliberately or otherwise) the New York Convention on this point and/or to assess evidence in a way that seems to favour defendants.

14
14579/04 and 12872/04, 11 April 2006, *Feyline* v. *Bashkirsk Petrochemical Company*.

15
A09-19423/04-20-16, *Veronica* v. *Kvadro*.

16
N F03-A51/05-1/2006, *Pacific Reliance* v. *Transmoreprodukt*.

17
A40-31732/07, 17 April 2008 and KG-A40/3758-08-P, 15 May 2008, *Loral Space and Communications Holdings Corp.* v. *Global Tel*.

C. Abuse of public policy

Allegations of violation of Russian public policy (or the 'fundamental principles of Russian law'[18]) are almost invariably found in pleadings submitted by defendants opposing the enforcement of awards by international arbitral tribunals in Russia.[19] Russian courts have in the past taken various approaches to this New York Convention ground for refusing enforcement. It has sometimes been confused with the interest of the Russian nation. In a 2003 case, for example, the federal *Arbitrazh* court for the Volgo-Viatsky Region refused enforcement of an ICC award as this could (among other things) lead to the defendant's insolvency, which in turn could 'negatively impact on the social and economic situation in Nizhny Novgorod'.[20] There have been times when the public policy ground has been used as a means of re-examining awards on the merits. In another 2003 case, for example, the federal *Arbitrazh* court for the Moscow Region held that an award ordering payment of damages to the claimant on an equitable basis following the invalidation of the underlying contract was contrary to the fundamental principle of 'equality of the parties', which required that each party should bear its own losses.[21]

On the other hand, *Arbitrazh* courts have tended to reject public policy arguments based purely on supposed errors of law or misinterpretation of evidence by arbitral tribunals. This is particularly true of the federal *Arbitrazh* court for the Moscow Region, which, as described above, is the cassation court most experienced in international arbitration. This court has on many occasions flatly rejected unconvincing public policy arguments.[22] With respect to awards of interest, supposedly excessive calculations based on contractual rates and/or foreign laws have also been considered as bearing on the merits, not on public policy.[23]

In short, *Arbitrazh* court practice has been mixed. The majority of decisions on public policy have been restrictive in their approach to this ground, but there have been notable, and often high-profile, exceptions.

Against this background, the Overview might have provided some useful clarification. Unfortunately, however, it has tended to obscure matters. Firstly, it emphasizes that public policy should not be used as a means of re-examining the substance of awards, which is encouraging. In paragraphs 12 and 20 of the Overview, it approvingly cites two cases in which cassation courts refused to set aside awards, or allowed their

---

18
The wording 'fundamental principles of Russian law' is used in the *Arbitrazh* Procedural Code (APC) as the equivalent criterion to 'public policy' with respect to international awards issued in Russia. Thus, the wording is viewed by most specialists as being identical in substance to public policy.

19
For a general description of the problem of public policy in this area of Russian judicial practice, see, W. Simons, 'The Enforcement of Foreign Arbitral Awards under Russian Law: the (Ab)Use of Public Policy Doctrine in Russian Courts' in Roger Clark (ed.) *International and National Law in Russia and Eastern Europe: Essays in Honor of George Ginsburgs* (London: Martinus Nijhoff, 2001) 373; B. Karabelnikov, 'Enforcement of Foreign Arbitral Awards in Russia', *Recht der Internationalen Wirtschaft* 2004, 22; V. Shaleva, 'The Public Policy Exception to the Recognition and Enforcement of Arbitral Awards in the Theory and Jurisprudence of the Central and Eastern European States and Russia' (2003) 19:1 *Arbitration International* 67.

20
17 February 2003, A43-10716, *United World* v. *Krasny Yakor*.

21
15 August 2003, KG-A40/5470-03P, *MMK* v. *Banka Polska*.

22
For example, on 15 June 2005, the federal *Arbitrazh* court for the Moscow Region rejected an application for an award to be set aside on the basis that 'the claimant disagrees with the tribunal's assessment of the evidence, but the *Arbitrazh* court is not entitled to re-examine the tribunal's decision on the merits and give another assessment of the facts and evidence which the tribunal investigated' (KG-A40/4342-05, *Kadila Pharmaceuticals* v. *Capital Care*).

23
Federal *Arbitrazh* court for the North-Western Region, 9 December 2004, A42-4747/04-13, *Dana Feed* v. *Arctic Salmon*; see also the Presidium of the SAC, 19 September 2006, 5243/06, *Joy-Lud* v. Moscow *Oil Refinery*, referred to *infra* note 56. In a judgment of 12 March 2008 (F03-A24/07-1/6043, *Czech Commerce Bank* v. *Kamchatgasprom*), the federal *Arbitrazh* court of the Far Eastern Region also held that an award including compound and punitive interest was not contrary to public policy.

enforcement, despite arguments advanced by the defendants that the arbitral tribunal misapplied Russian law or misunderstood the facts. Although largely uncontroversial for experienced arbitration practitioners, these decisions concern domestic awards, and the Overview seems to rely to some extent in its reasoning on a provision in the 2002 law on arbitration in the Russian Federation (which applies only to domestic awards), which expressly forbids the enforcing court to 'investigate the facts established by the tribunal or re-examine the substance of the award'. Ideally, the Overview might have chosen as one of its examples a case relating to enforcement of a foreign award, in order to make it clear that such limitation extends to international arbitration, too.

Secondly, despite these reminders of the limitations on the public policy ground, the Overview goes on to refer to public policy in relation to international awards in two cases (paragraphs 29 and 30), in both of which enforcement was refused. These cases seem to send precisely the opposite signal to that conveyed by the analysis in paragraphs 12 and 20.

In the first case, the foreign claimant was awarded $20 million in damages under a joint venture agreement with its Russian partner. Enforcement was refused by the Presidium of the SAC apparently because the damages payable by the Russian partner were assessed as equivalent to the foreign party's contribution to the joint venture, which meant that the foreign party might recover double the amount if the joint venture were subsequently wound up.[24] That seems at least logical (if questionable) as a rationale for refusing enforcement, although it may be wondered whether the award itself allowed for such a scenario.[25] More significantly, however, the SAC obscured the underlying logic of its refusal by referring to a host of other clearly irrelevant factors. Among other things, it criticized the earlier courts for not taking into account the fact that the capital contribution by the foreign company had been made in kind rather than in cash, and for not considering whether the tribunal had properly investigated whether the contribution had actually been made by the foreign investor. Both these issues (to the extent they are relevant) clearly go to the merits and should not be re-examined. Finally, the SAC also chose to describe the concept of public policy as being 'based on principles of equality of parties to civil-legal relationships, on good faith in their conduct, on the proportionality of civil liability with the consequences of the breaches, taking into account the fault of the parties.' This surprising definition has no apparent basis in Russian legislation or doctrine. Reading between the lines (and judging from the fact that the Overview mentions the amount of the award in this case), the SAC appears to wish to retain residual jurisdiction to assess the 'proportionality' of all awards against Russian parties on the basis of Russian criteria. Again, this hardly tallies with its stated conservatism with respect to public policy in paragraphs 12 and 20.

The second public policy case cited in the Overview (paragraph 30) is arguably correct given the facts as described, although it may be wondered whether those facts are complete and whether the decision opens the floodgates to a new type of defence in Russia. In this case, the defendant obtained proof, after the award was issued, that the

---

24
The facts are unclearly set out in the Overview, so this is to some extent the authors' own interpretation of the case description.

25
The facts of the case cited in paragraph 29 of the Overview are similar to those decided by the Presidium of the SAC on 14 January 2003 (case no. 2853/00, *Pressindustria* v. *Tobolsk Petrochemical Combine*). In the latter case, the SAC refused enforcement of a foreign award ordering a Russian joint-venture partner to return to the foreign investor the latter's capital investment, as the award amounted to de facto liquidation of the joint venture. However, the SAC failed to take account of the fact that the arbitral tribunal reserved jurisdiction in its award to order the foreign investor to return to the Russian party any future proceeds from the liquidation of the JV, precisely to prevent double recovery.

claimant company was not registered (i.e. did not exist) during the period when the losses in question were incurred. The Presidium of the SAC overturned the previous decisions allowing enforcement of the award and referred the case back to the first instance court, as 'new facts had emerged' and allowing enforcement in such circumstances would be a breach of public policy. The Presidium seems to have been influenced by the idea that the underlying contract was fraudulent and/or that the claimant had acted in bad faith, even though this conclusion does not necessarily follow from the facts. It is not hard to see that the net effect of creating a 'new facts' defence may be to allow defendants to raise allegations that were not put to the arbitral tribunal and which go to the substance of the award.

Both of the above negative decisions by the SAC are questionable on their face, are awkwardly reasoned and seem to reflect hostility towards international arbitration that cannot find expression within the confines of the New York Convention. It is regrettable—although significant—that the SAC chose to include them in the Overview. They show that public policy arguments still have teeth in Russia.

Since the publication of the Overview, there have been two key decisions by *Arbitrazh* courts relating to public policy: one positive, the other negative.

In a decision dated 26 May 2006, the Presidium of the SAC made a key ruling in favour of enforcement, more or less in keeping with the logic of its pro-arbitration guidance in paragraphs 12 and 20 of the Overview. A Dutch claimant that had lent money to a Russian company obtained a number of arbitration awards in its favour, which it tried to enforce. Having been successful at first instance it was denied enforcement at cassation level by the federal *Arbitrazh* court for the Eastern Siberian Region, which held that there was no proof that the monies had actually been advanced and that therefore enforcement would be a breach of public policy. The SAC Presidium overturned the cassation court's decision and re-instated the first instance judgment allowing enforcement.[26] It held that there was no reason for considering that public policy would be breached if enforcement were allowed, and it further held that the cassation court had wrongly re-examined the arbitral tribunal's factual findings on the advance of the loan monies, as this fell within the arbitral tribunal's jurisdiction.

In a decision dated 25 May 2006,[27] the federal *Arbitrazh* court for the Volgo-Viatsky Region refused to enforce an award in favour of a company from the British Virgin Islands, Unimpex Enterprises Ltd., ordering the Russian defendant to pay the claimant $21.5 million as contractual damages for failure to transfer shares, on the grounds that, among other things, the damages greatly exceeded the value of the shares and were punitive in nature, and the tribunal should have applied Article 333 of the Russian Civil Code to reduce the contractual damages.[28] Although it was true that the damages greatly exceeded the value of the shares, this was because more than six years had elapsed since the start of the contract. As regards Article 333 of the Civil Code, its application is discretionary so there is no question of its being considered a mandatory rule of Russian law. It remains pure guesswork why failure to apply this article could be considered a breach of Russian public policy. This decision has not been the subject of a supervisory review by the SAC.

26
4438/06, 26 May 2006, *Arduina* v. *UVGK*. The various judgments in this case were published in *Mezhdunarodny Kommerchesky Arbitrazh* 2007/1, 112 (in Russian).

27
A82-10555/2005-2-2, *Unimpex* v. *NPO Saturn*.

28
Article 333 of the Civil Code of the Russian Federation (Reduction of a Penalty) provides that 'if a penalty which has become payable is clearly disproportionate to the consequences of violating an obligation, a court has the right to reduce the penalty'. It is assumed that the applicable law of the contract in this case was Russian.

Overall, the picture that emerges is still mixed. On the one hand, there are a large number of creditable decisions from *Arbitrazh* courts displaying a restrictive approach to the public policy ground that is in keeping with international practice. On the other hand, *Arbitrazh* courts at all levels—including the SAC—sometimes issue nonsensical or clearly incorrect judgments based on apparently protectionist and anti-arbitration instincts, especially where high-value awards are concerned. Russian defendants are likely to go on trying their luck with this defence.

D. Public policy and incompatible local decisions

Perhaps the most widespread and notorious tactic adopted by Russian defendants anxious to avoid paying a future arbitral award is to instigate a claim by a third party in the State courts with a view to having the underlying contract declared invalid. If such a claim is successful, then enforcement of any subsequent arbitration award that conflicts with the court decision (i.e. an award finding that the contract is valid) will be deemed contrary to public policy.

Space does not permit an exhaustive analysis of the circumstances in which such third party claims can be brought under Russian corporate law, but they are numerous.[29] The main risk for foreign counterparties is shareholder claims (referred to in Russian legal writing as *kosvenniye iski* or 'indirect claims'), whereby a holder of a Russian company's shares applies to a court seeking the invalidation of either so-called 'major transactions' (i.e. transactions involving more than 25% of the total assets of the company) entered into by the company's management without the requisite approval of shareholders,[30] or 'interested party transactions' (transactions with an affiliate of a shareholder or in which a member of the company's board of directors has a personal interest), again lacking the necessary approval from the non-interested members of the company's board of directors, or in some circumstances, from the shareholders. Similar actions may be brought where the validity of the corporate document approving the relevant transaction is called into question (for example, the validity of minutes of board meetings). Russian law does not contain the same protections for bona fide counterparties to contracts with limited companies as, for example, English law, and it is difficult, if not impossible, for a counterparty to protect itself fully against such claims. What particularly surprises foreign counterparties is that it makes no difference under Russian law whether the shareholder that brings the indirect claim is in the same beneficial ownership as the Russian company that concluded the contract.

An example of an indirect claim is provided by the 2003 case of *Quality Steel* v. *Bummash*. In 2000, Quality Steel, a company based in the British Virgin Islands entered into several contracts with Bummash, a Russian company. These contracts referred disputes to arbitration in Holland under the Arbitration Rules of the Netherlands Arbitration Institute (NAI). When a conflict emerged and Quality Steel sought to institute arbitration, a shareholder of Bummash, Uralskiye Zavody, which was also affiliated to Bummash, applied to the local *Arbitrazh* court for a declaration that the contracts in question were null and void as they were interested party transactions made without the necessary corporate approval (a member of the board of directors of Bummash had failed to inform the company that he also occupied the same position in a company

29
For an account of these circumstances see V. Khvalei, 'The Effect of Parallel Litigation Under Russian Law', *Global Arbitration Review*, vol. 3, issue 2 (2008) 26.

30
Transactions falling within the 'ordinary course of the company's business' are an exception to this rule.

affiliated to Quality Steel). The federal *Arbitrazh* court for the Urals Region invalidated the contracts in two judgments dated 29 December 2003 and 24 December 2004.[31] The latter judgment accused Quality Steel, not Bummash, of being 'in breach of Russian law'. When Quality Steel approached the Russian courts for enforcement of the NAI award in 2005, it met with a refusal owing to the existence of conflicting Russian court decisions.[32]

The jurisdictional problem posed by such indirect claims where the contract includes an arbitration clause is unfortunately compounded by a surprising degree of uncertainty in Russian corporate law and in judicial practice with respect to such claims. A restrictive application of Russian law would protect the legitimate expectations of contractual counterparties, yet Russian courts sometimes seem to be oblivious to the commercial consequences of their decisions. For example, the SAC has made it clear that shareholders bringing indirect claims must demonstrate that their interests have been damaged as a result of the contract.[33] In practice, however, the *Arbitrazh* courts rarely give any consideration to this issue (in the *Quality Steel* v. *Bummash* case, for example, Uralskiye Zavody provided no evidence of such damage to its interests). Furthermore, the law arguably requires shareholders to request not only a declaration that the contract is void but also an order for restitution of any payments made pursuant to the contract. Such an order might provide partial compensation to the foreign counterparty. However, these orders are practically never requested, nor do Russian courts take the initiative of ordering restitution in the absence of a request.[34]

In theory, an international arbitral tribunal hearing a claim based on a contract that is invalid under Russian law because the Russian party failed to obtain the necessary approvals can of course decide that the contract is invalid, just as the Russian court hearing the concurrent shareholder claim can. However, where the law of the contract is not Russian, an arbitral tribunal may legitimately apply notions such as apparent authority or estoppel to rescue the contract, whereas a Russian court, applying Russian conflict rules, will generally consider the question of the authority of a signatory on behalf of a Russian company to be governed purely by Russian law, irrespective of the law chosen by the parties.[35] This makes a collision between the two decisions not only possible but likely.

It is the view of the present authors that, apart from a more consistent and restrictive application of existing corporate law, a more fundamental solution to the problem is required. In the first place, Russian law should treat shareholders as being bound by the arbitration clause in the underlying contract, and thus refuse even to hear such claims. Interestingly, this was the conclusion reached by the *Arbitrazh* courts in the *Duke Investments* case (see section II(B) below) in relation to claims brought by the public prosecutor. Secondly, the courts should abandon the idea that enforcing an award that is in contradiction with an existing Russian court judgment is necessarily contrary to public

---

31
F09-3778/03-GK (29 December 2003) and. F09-4269/2004-GK (24 December 2004).

32
Federal *Arbitrazh* court for the Urals Region, 12 October 2005, F09-2110/05-C6.

33
On 18 November 2008, the Plenum of the SAC published decree no. 19 entitled 'Various Questions relating to the Application of the Federal Law on Joint-Stock Companies'. Paragraph 38 of the decree provides that 'claims by shareholders seeking a declaration of the invalidity of transactions concluded by joint-stock companies may be allowed where proof is provided that the rights and lawful interests of the shareholder have been damaged'.

34
For a critical analysis of Russian corporate law and its application by Russian courts in relation to shareholder claims, see B. Karabelnikov 'Indirect Claims as a Mechanism for Allowing Russian Companies to Breach Their Own Obligations', published in July 2007 in the journal *Zakoni Rossii* and the database *ConsultantPlus* (in Russian).

35
Article 1202.2(6) of the Russian Civil Code provides that the personal law of an individual or legal entity governs the process whereby the individual or entity obtains civil law rights and enters into civil law obligations.

policy. However, Russian jurisprudence is unlikely to develop in either of these directions in the near future.

E. Expanding the category of non-arbitrable claims

Like many other laws, Russian law contains no comprehensive definition of what disputes are or are not arbitrable. In Article 248 of the *Arbitrazh* Procedural Code, it does however contain a list of disputes that are reserved for the 'exclusive' jurisdiction of the state *Arbitrazh* courts. They include disputes involving non-Russian parties:

(1) which 'relate to property owned by the state' (including claims linked to the privatization of state property);
(2) 'the subject matter of which is real estate located in the Russian territory';
(3) which are connected to the registration or granting of patents, trademarks or industrial models;
(4) which concern applications for a declaration that entries made in state registers are invalid; and
(5) which relate to the creation, liquidation and registration in Russia of legal entities and which challenge the validity of decisions made by the organs of such legal entities.

The wording and context of Article 248 clearly show that its purpose is to prohibit the resolution of certain disputes by foreign State courts, not arbitral tribunals. Such an interpretation is consistent with the corresponding provisions of laws in other countries, for example Germany.[36] Nevertheless, *Arbitrazh* courts have in the past often relied on Article 248 of the *Arbitrazh* Procedural Code as listing non-arbitrable matters for the purpose of Article V.2(a) of the New York Convention. This approach has been criticized by Russian commentators.[37] Most authors agree that any private civil law dispute may be referred to arbitration (with the sole exception of claims for bankruptcy, which the 2002 insolvency law expressly designates as non-arbitrable). Disputes related to public or administrative law (such as those relating to regulatory matters) are not arbitrable, however.

In its Overview, the SAC seems to endorse the latter view. It cites two cases relating to non-enforcement of foreign arbitral awards on grounds of non-arbitrability (paragraphs 27 and 28). In both cases it follows the private law/public law reasoning rather than reliance on Article 248 of the *Arbitrazh* Procedural Code. However, the specific facts of those cases give cause for concern.

Both cases relate to real property located in Russia. In the first case, according to the Overview, the tribunal 'recognized the right of ownership' of the claimant over the property and—surprisingly—'obliged the registering authority to register this right'. Enforcement was therefore refused. Clearly such an award presents problems and the court decision is perhaps not surprising. However, it hardly seems likely that an arbitral

---

36
Geimer in Zöller, ed., *Zivilprozessordnung*, 23d ed. (2002), § 1030 note 4; Münch in *Münchener Kommentar zur Zivilprozessordnung*, vol. 3, 2d ed. (2001), § 1030 note 2, 17; Lachmann, *Handbuch für die Schiedsgerichtspraxis*, 2d. ed. (2002) note 207; Schwab/Walter, *Schiedsgerichtsbarkeit Kommentar*, 6th ed. (2000) 37; Schlosser in Stein-Jonas, eds., *Kommentar zur Zivilprozessordnung*, vol. 7/II, 21st ed. (1994), § 1025 note 27d., Poudret/Besson, *Droit comparé de l'arbitrage international* (2002), note 345ff.

37
See B.Karabelnikov & A.Makovsky 'Russian Approach to the Problem of Arbitrability of Disputes' in A. Trunk, R. Knieper, A. Svetlanov, eds., *Festschrift für Mark Moiseevic Boguslavskij* (BWV, 2004) 285 (in Russian); A.Zhiltsov, 'Challenging of International Arbitral Awards Under Russian Law', *Mezhdunarodny Kommerchesky Arbitrazh* 2005/1, 16 (in Russian); A.Nesterenko 'Criteria for Arbitrability of Disputes Under Laws of the RF'. *Mezhdunarodny Kommerchesky Arbitrazh* 2005/4, 30 (in Russian).

tribunal would order a third party, least of all a state body, to do anything, so the accuracy of the SAC's restatement of the case in the Overview must regrettably be questioned. It seems more likely that the award simply ordered the defendant to transfer title. That is clearly a private civil law matter which, following the analysis set out above, should be arbitrable.

The second case cited in the Overview relates to an award that apparently authorized the claimant as mortgagee to sell property owned by the defendant in order to recover damages. Again, although this award concerns (in part) real property, it is difficult to see why it relates to a public/administrative law relationship.

In a decision by the federal *Arbitrazh* court for the Western Siberian Region dated 9 March 2006, the SAC's methodology as set out in the Overview was simply ignored. The court declined to enforce an award issued by MKAS requiring a Russian lessee to pay rent to a foreign lessor for property located in Russia. It applied Article 248 of the *Arbitrazh* Procedural Code and ruled that the arbitral tribunal had decided a non-arbitrable matter.[38]

Regardless of whether *Arbitrazh* courts apply Article 248 of the *Arbitrazh* Procedural Code or the private law/public law reasoning, it appears that foreign investors will continue to face risks with regard to awards whose 'subject matter' is real estate located in the Russian Federation. Not only cases determining title to property, but apparently also disputes concerning the payment of rent may fall foul of this principle. Indeed, possibly even disputes over the ownership of legal entities that in turn own real estate in Russia could be deemed non-arbitrable. It is likely that this category will go on expanding.

II. Well-known cases concerning enforcement of foreign awards decided by Russian courts between 2005 and 2007

As mentioned above, Russian law is not formally a precedent-based system. Judgments by state *Arbitrazh* courts are often inconsistent in their legal analysis, as the above analysis has demonstrated. Unless a decision on a relevant issue has been rendered by the Presidium of the SAC, Russian judges are reluctant to heed the cases decided by their colleagues. However, an analysis of case law to some extent allows Russian litigators to prepare for likely arguments from defendants and pre-empt objections made by the enforcing court. In this section we analyse three recent high-profile cases concerning the enforcement of foreign arbitral awards. These cases illustrate some of the issues already discussed in section I. More importantly, however, they demonstrate that judicial decision-making is not only unpredictable, but also sometimes depends on the political standing of the parties and/or other forms of influence.

A. Yukos—predator turned victim

The bankruptcy of Yukos, and in particular the treatment Yukos and its executives have received in the Russian civil and criminal courts, has received wide attention in the Western media. What is perhaps less well known is that, before the breakdown of relations between Mr Khodorkovsky and the then President Putin, Yukos met with

38
F04-786/2006, *Belavia* v. *Sibir*.

significant success in opposing enforcement of international arbitral awards in the Russian courts.

In 1993, Yukos and a Turkish company, Tupras (Turkish Petroleum Refineries, Inc.), entered into a contract for the supply of crude oil, which included an ICC arbitration clause. A conflict arose and the Turkish buyer commenced arbitration proceedings. In 2000, an ICC arbitral tribunal awarded it some $2.4 million plus interest. However, the Russian courts declined to enforce the award due to uncertainty over whether the award had entered into effect and whether the arbitration agreement existed. The courts' reasoning, as expressed in a judgment of the federal *Arbitrazh* court for the West Siberian Region dated 6 August 2003,[39] was as follows:

> Another reason for refusal of enforcement [apart from the fact that the ICC award had not entered into effect] was the failure of the applicant to prove the existence of the agreement to submit disputes arising under the contract of 25 December 1993 to international commercial arbitration.
>
> This conclusion is based on the fact that there is no original of the power of attorney issued by the debtor [i.e. Yukos] in the name of Murat Hallah, authorizing him to act on behalf of Yukos, and the photocopy of this power of attorney shows an address for that company which is different from its address stipulated in its Charter. Also, no proof was submitted evidencing the authority of Mr Eduard V. Grushevenko, who also signed the contract on behalf of Yukos. Based on the foregoing, the court reasonably concluded that the international commercial arbitration exceeded the scope of its competence because the arbitration agreement signed by improper persons had no legal significance.

The Presidium of the SAC left this judgment intact.

It would appear from the above that, although it did not have the onus of proving the authority of the individuals who had signed the arbitration agreement, the Turkish claimant nevertheless managed to produce a photocopy of the power of attorney issued by Yukos. However, the Russian judges did not accept it because it was a mere photocopy, rather than the original, and because it bore an address that did not coincide with the address shown in Yukos' Charter.[40] To say that the courts' reasoning was in breach of the New York Convention would be an understatement.

Since Yukos' fall from grace at the end of 2003, not a single case of significance has been decided in its favour in the Russian courts.[41] In 2006, a MKAS tribunal awarded Yukos Capital S.a.r.l., a Luxemburg-based affiliate of Yukos, some $490 million from YNG, a former affiliate of Yukos. The debt arose from loans provided by the Luxemburg affiliate to YNG, which was subsequently acquired by Rosneft, a State-owned company. Rosneft therefore found itself in the position of having inherited YNG's debts. Four separate awards were rendered by the MKAS tribunal, providing for termination of the loan agreements and ordering YNG (i.e. in effect Rosneft) to return the funds with interest.

39
F04/3755-580/A75-2003.

40
Russian law does not require powers of attorney issued by companies to indicate their official registered address. A power of attorney issued by a legal person under Russian law must contain the signature of the authorized person, the corporate seal and the date of its issuance. All other features (including letterhead, address, etc.) do not affect its validity.

41
One exception to this rule, which is sometimes cited as supposed proof of the independence of the Russian courts, is a decision of the Presidium of the SAC dated 19 June 2007 (case no. 15954/06), which overturned two previous judgments refusing enforcement of an award in favour of Moravel Investments against Yukos (Moravel was the assignee of Société Générale, which had lent several hundred million dollars to the Russian company). It is argued that this decision demonstrates a willingness to allow Yukos creditors to make a recovery against the company. However, the fact that the Presidium of the SAC simply referred the case back to the lower courts, without itself ruling in favour of enforcement, means that, to best of the authors' knowledge, Moravel was in fact unable to obtain a final decision on enforcement before Yukos was finally wound up.

The *Arbitrazh* court for the City of Moscow issued two judgments on 18 May 2007, each setting aside two of the four awards.[42] Although made by two different judges, both judgments are almost identical in their wording. They rely on three separate grounds: (i) the arbitral tribunal did not give the defendant enough time to present its case when refusing to postpone the hearing, (ii) prior to the hearing, the arbitral tribunal allowed the claimant to add new claims for the termination of the loan agreements and return of the principal to its original claims for damages and interest; and (iii) the arbitrators were not impartial because two of them had been speakers at a seminar partly sponsored by the law firm representing the claimant and had attended another such seminar, and the concealing of these facts from the defendant violated Russian public policy.

Little can be said by way of useful commentary on such reasoning. Criticism levelled by *Arbitrazh* court judges at procedural decisions made by MKAS arbitrators is generally misplaced and the observations here concerning the tribunal's refusal to delay the hearing and its acceptance of additional claims are no exception (it may be added that the respondent apparently never raised such arguments before the tribunal itself). As for the matter of partiality, the court's findings are plainly untenable, given that the seminars in question were attended by several hundred people.

The above decisions were left intact by the federal *Arbitrazh* court for the Moscow Region in two decisions dated 26 July 2007.[43] The only slight modification it made was to overturn the public policy finding of the first instance court, considering instead that grounds (i) to (iii) above were breaches of the arbitral rules agreed by the parties (hence, apparently, of Article V.1(d) of the New York Convention). The decisions of the federal *Arbitrazh* court were, in turn, upheld by the SAC in a decision dated 10 December 2007.[44]

This was not the only defeat sustained by Yukos in the Russian courts in an arbitration-related matter. Earlier in 2006, the *Arbitrazh* courts ruled that a 2004 agreement between YNG (at the time owned and controlled by Yukos) and Société Générale, whereby YNG stood surety for repayment of a loan granted by the bank to Yukos, was void *ab initio*.[45] This was an indirect claim submitted by YNG's new shareholder, Rosneft. Consequently, if ever an arbitration award is issued ordering YNG (i.e. Rosneft) to pay the amount secured, the award will have little chance of being enforced in Russia.

B. The Kaliningrad case—the role of local politics

This saga began in 1997, when the government (*administratsia*) of the Kaliningrad Region obtained from Dresdner Bank AG a $10 million loan for certain agricultural projects. Kaliningrad is an enclave isolated from the rest of Russia, located in the former territory of Eastern Prussia. It may be for reasons of geographical proximity that a German bank decided to lend money to a Russian regional government.

The loan was expressly approved by Kaliningrad's parliament (*Duma*) and the federal authorities (Ministry of Finance), despite the fact that Russian legislation at that time was

---

42
A40-4577/07-8-46, A40-4582/07-8-47 and A40-4576/07-69-46, A40-4581/07-69-47, *Rosneft* v. *Yukos Capital S.a.r.l.*).

43
Federal *Arbitrazh* court for the Moscow Region dated 26 July 2007 Nos. A40/6775-07 and A40/6616-07.

44
14956/07.

45
Arbitrazh court for the City of Moscow, 22 March 2006, A40-69739/05-1-362, *Rosneft* v. *Moravel Investments*, confirmed by 9th *Arbitrazh* court of appeal, 22 May 2006, 09-AP-4207/2006-GK and federal *Arbitrazh* court for the Moscow Region, 7 September 2006, KG-A40/7419-06.

far from clear on the need for such approvals. On the basis of those approvals, the loan agreement was executed by the local governor, Mr L. Gorbenko.

Local elections subsequently took place, leading to the designation of a new governor, Mr V. Yegorov. The new administration declined to repay the loan. At that point, the bank assigned its rights to a Cypriot company, Duke Investments Ltd, which commenced an arbitration in accordance with the arbitration clause in the loan agreement.[46]

The defendant participated in the arbitration (although it declined to appoint its own arbitrator) and argued that the loan agreement was void *ab initio* as the former governor, Mr Gorbenko, had exceeded his authority and that the arbitration clause it contained was thus void, too. Not surprisingly, the tribunal rejected both arguments and ordered the government to repay the principal and interest amounting to approximately $20 million.

Immediately after the award, the public prosecutor in Kaliningrad began proceedings in the Kaliningrad courts with a view to having the underlying loan agreement declared invalid under Russian law on the ground that it was a fraudulent transaction. Russian procedural law allows the public prosecutor to bring such a claim in the interests of a State-owned signatory to the contract. On 20 January 2005 the *Arbitrazh* court for the Kaliningrad Region refused jurisdiction over the public prosecutor's claim, as the defendant (Duke Investment) had requested the matter be referred to arbitration in accordance with Article II of the New York Convention. The court specifically mentioned that the public prosecutor was bound by the arbitration clause in the loan agreement. This judgment was confirmed by the federal *Arbitrazh* court for the North-Western Region in a decision dated 23 September 2005.[47]

After such a show of support from the courts for the foreign claimant, and for international arbitration as an institution, one might have expected the award to proceed to enforcement without further difficulty. In 2005, however, Mr Yegorov was replaced by a new governor, Mr G. Boos. Unlike his predecessor, Mr Boos had significant political support from Moscow (he was a former federal tax minister), and upon his appointment Duke Investment's fortunes took a turn for the worse.[48]

On 3 March 2006, the *Arbitrazh* court in the Kaliningrad district declined to enforce the award on the following grounds: (i) the loan agreement required the Kaliningrad regional *Duma* to make advance provisions in the regional budget, which is contrary to Russian constitutional law; (ii) the failure to include the Kaliningrad regional *Duma* (as opposed to the Kalingrad government) as a party to the arbitration breached Article 6 of the European Convention on Human Rights (right to a fair hearing); (iii) such failure was also a failure properly to inform a party to the arbitration of the hearing, in accordance with Article V.1(b) of the New York Convention; (iv) enforcement of the award would breach Article 1 of Protocol No. 1 to the European Convention on Human Rights (right to peaceful enjoyment of possessions); and (v) the arbitral tribunal had been improperly constituted in violation of Article V.1(d) of the New York Convention.

The judgment of the *Arbitrazh* court in the Kaliningrad district was confirmed by the federal *Arbitrazh* court for the North-Western Region on 3 May 2006.[49] It was also left

46
The loan agreement also contains an extensive waiver of state immunity by the Kaliningrad government, including immunity from execution.

47
A21-2499/03-C1, *Duke Investments* v. *Kaliningrad*.

48
Former governor, Mr Gorbenko, was himself prosecuted for abuse of authority; all the Russian lawyers who attended the arbitration hearings in London were interrogated by the Russian investigating authorities.

49
A21-5758/2005.

intact by the SAC, which declined even to exercise its supervisory jurisdiction to review the case.[50]

The federal *Arbitrazh* court for the North-Western Region admittedly examined in greatest detail the fifth ground mentioned above, which seems to have been at the centre of the case. It appears that the arbitration agreement provided that the LCIA could appoint the chairman of the arbitral tribunal if the party-appointed arbitrators could not agree. It did not, however, provide that the LCIA was the 'appointing authority' under the UNCITRAL Arbitration Rules. The LCIA in fact appointed the second arbitrator after the Kaliningrad government failure failed to do so. This was, technically, a breach of the arbitration agreement, as such appointment should have been made by an authority designated by the Permanent Court of Arbitration in The Hague (under Article 7.2.(b) of the UNCITRAL Arbitration Rules).

The hostile attitude of the courts is nonetheless evident in the implausible interpretation of the European Convention on Human Rights by the *Arbitrazh* court of the Kaliningrad district, which was not corrected by either of the superior courts. It is difficult to avoid the conclusion that this attitude was connected with the political influence of the new governor of the Kaliningrad district.

C. *Joy-Lud* v. *Moscow Oil Refinery*—some foreigners succeed

The *Joy-Lud* litigation provides a particularly colourful illustration of the various pitfalls of enforcement proceedings in Russia.

On 19 January 1995, the Moscow Oil Refinery (a Russian company) and Joy-Lud Distributors International (a US company) entered into a contract for the supply of diesel oil by the Refinery to Joy-Lud during the period 1995–2004. The contract was subject to Swedish law and provided for *ad hoc* arbitration in Stockholm. In 1997, the parties made addendum no. 28 to their contract, which provided for the payment of a fine[51] by the Refinery if it failed to perform its obligations.

The Refinery subsequently came under the indirect ownership of the Moscow City government. The seller ceased delivering the diesel oil and Joy-Lud commenced arbitration.

The Refinery brought various indirect claims in the Moscow City *Arbitrazh* court, with a view to having the contract declared invalid, so as to forestall enforcement of any arbitral award. The first such claim was made by the public prosecutor of the City of Moscow; later, other similar claims were made by new shareholders of the Refinery. All of these indirect claims failed: the public prosecutor's claim because the Refinery was not a State-owned enterprise,[52] and the claims of the new shareholders of the Refinery because they were not shareholders at the time the contract was concluded.[53]

50
A more extensive commentary on those judgments may be found in V. Yarkov 'Denial of Enforcement of the London Award of International Arbitration (Continuation of the Kaliningrad Case)' *Mezhdunarodny Kommerchesky Arbitrazh* 2007/2, 67 (in Russian). The full texts of the Russian court judgments in this matter are published in the same edition of that journal.

51
The Russian term for fine (*shtraf*) is used in the judgments to refer to the provision of the addendum. It is not known whether different terminology was used in English (e.g. 'liquidated damages').

52
Judgment of the *Arbitrazh* Court of the City of Moscow dated 8 December 2004 no. A40-29339/04-40-332.

53
Federal *Arbitrazh* court for the Moscow Region, 12 April 2006 KG A40/71-06.

Meanwhile, on 14 June 2005, the Stockholm arbitral tribunal awarded Joy-Lud $28 million in damages based on the fine specified in addendum no. 28. The Russian courts refused to enforce this award on the ground that the fine was greater than the real loss to the claimant and was punitive in nature, whereas Russian law requires an element of 'proportionality' (*sorazmernost'*) in damages, as laid down in Article 333[54] of the Russian Civil Code. The courts accordingly held that enforcement of the award would contravene public policy.[55]

Joy-Lud did not give in, however. It applied to the SAC for a supervisory review, which the SAC agreed to carry out. The Presidium of the SAC concluded that the application of a contractual fine could not in itself amount to breach of Russian public policy since such fines are expressly permitted under Article 330 of the Russian Civil Code. The Presidium enforced the award without returning the file to a lower court for reconsideration.[56]

The Moscow Oil Refinery might well have been expected to give up at this stage, but it was not to be so. The shareholders of the Refinery submitted a new claim, asking for addendum no. 28 to the contract, as opposed to the contract itself, to be declared invalid. As the shareholders had undeniably acquired their shares before the addendum was signed, timing could this time not be used as a barrier to the claim. The federal *Arbitrazh* court for the Moscow Region granted the claim and addendum no. 28 was declared void *ab initio* on the ground that it was a major transaction that had not received the requisite shareholder approval.[57] Consequently, by the time the 19 September 2006 decision of the Presidium of the SAC allowing enforcement of the Swedish award was made, the underlying contract (specifically the addendum providing for the fine to be paid) had already been invalidated by a Russian court judgment.

That might have been decisive but for one final twist. On 28 November 2006, the Presidium of the SAC quashed the judgments of the *Arbitrazh* courts that had declared addendum no. 28 to be void. It rejected the shareholders' claims, among other reasons because the shareholders had failed to prove that their interests had been damaged by the conclusion of the addendum and the addendum was in any event concluded by the Refinery during the ordinary course of its business and so could not fall foul of the 'major transaction' rule.[58]

The story therefore ended happily for the foreign claimant (at least so far). However, a number of factors make it somewhat less reassuring than at first sight. First, not all foreign companies are prepared to spend time and money in the Russian courts trying to prevent vexatious parallel litigation aimed at preventing future enforcement. Secondly, although the reasoning of the Presidium of the SAC in its 28 November 2006 decision concerning the need for a shareholder claimant to prove that its interests had been damaged is correct, as mentioned earlier, this is an element that the SAC and the lower *Arbitrazh* courts generally do not bother to consider. Thirdly, on both occasions when

---

54
See *supra* note 28. As already explained, this article could in no way be considered constitutive of Russian public policy, since its application by Russian judges is purely discretionary. (It may be added that in the case in question the law of the contract was Swedish law, so Article 333 was not directly applicable.)

55
Arbitrazh court for the City of Moscow, 15 December 2005, A40-64205/05-30-394, confirmed by federal *Arbitrazh* court for the Moscow Region, 21 March 2006, KG-A40/922-06. The judgments of the Russian courts in the *Joy-Lud* case were published in *Mezhdunarodny Kommerchesky Arbitrazh* 2007/1 & 3 (in Russian).

56
5243/06, 19 September 2006.

57
Federal *Arbitrazh* court for the Moscow Region, 26 June 2006, KG- A40/5569-06.

58
9148/06.

the Presidium of the SAC intervened, it made a final judgment on the case without referring the case to a lower court for reconsideration, as normally happens when it overturns decisions. Quite why Joy-Lud merited such special treatment is not clear, but this is certainly exceptional.

III. General recommendations and conclusions

The picture of Russian law and Russian justice painted by the above analysis is far from attractive. If the decision on whether or not to invest in Russia or do business with Russian companies is determined by the level of available legal protection in the Russian courts, few parties would be likely to proceed. However, commercial advantages sometimes outweigh legal risk. Many foreign parties are effectively obliged to run the gauntlet of Russian justice, at least at the stage of enforcing an eventual arbitral award, and are more interested in knowing what steps they can take to improve their chances of success than in hearing how difficult it will be. Below, the authors propose a number of measures that may be of some practical assistance. They do not wish to suggest that these measures will guarantee a positive result, but rather that there are ways and means of avoiding problems and assuaging the sensibilities of the enforcing court. Parties can thus maximize their chances.

It may be added that some of the measures below are relevant not only to parties but also to arbitral tribunals. Arbitrators are duty-bound to render awards that are, as far as possible, enforceable. Even if claimants are trapped through their ignorance of Russian court practice, arbitrators should try to assist meritorious claims by forestalling possible objections at the enforcement stage.

At the stage of signing the contract:

1. Avoid, where possible, making agreements that are contrary to any provisions of Russian law that may be viewed as mandatory by the Russian courts, especially Russian corporate law concerning the governance of companies registered in Russia. Foreign shareholders in such companies frequently make agreements that, for example, limit their right to nominate candidates to the board or to sell shares in ways that contradict Russian law. In making such agreements subject to foreign laws and to the jurisdiction of foreign tribunals, they may hope to avoid the application of Russian law altogether (or may simply be ignorant of Russian law). However, Russian courts are likely to take a hostile view of such contracts. At the request of any party adversely affected by them, they may—rightly or wrongly—declare them invalid[59] or refuse to enforce awards relating to them, on the ground that they contravene pubic policy.[60]

2. Obtain as many documents as possible demonstrating that the Russian signatory or signatories have the necessary authority to conclude the contract on the company's behalf. Bear in mind that the burden of evidence is likely to be much heavier at the

---

59
It may be noted that actions for declarations that contracts are null and void on public policy grounds may be brought by any party whose interests are adversely affected by the contract under Russian law, not merely by a shareholder. The category of potential claimants is therefore wider than the category of potential claimants where the contract is alleged to be a major or interested party transaction.

60
For example, on 31 March 2006, the federal *Arbitrazh* court for the Western Siberian Region upheld two lower instance judgments declaring a shareholders agreement between foreign shareholders of a Russian company to be void on public policy grounds. In that case, the shareholders had made the agreement subject to Swedish law. In the eyes of the court, that fact was in itself enough to contravene public policy (*Avenue and others* v. *CT Mobile and others*, F04-2109/2005 14105-A75-11, published in *Mezhdunarodny Kommerchesky Arbitrazh* 2007/3, 98 (in Russian).

enforcement stage than before the arbitral tribunal. These documents should normally include certified copies of the company's documents of incorporation, certified copies of corporate documents relating to the appointment of its management (general director, board of directors), original(s) of power(s) of attorney issued for the person(s) signing the contract (if this person is not the general director), an original of the company's statement of accounts (*balans*) dating from the end of the month immediately before the contract was signed (for the purpose of disproving that the contract was a major transaction), and two original extracts from the Joint State Register of Companies of the Russian Federation (one for the date of execution of the contract in question and the other for the date of performance of the main obligation (if these dates are not the same)). The former extract may be necessary to prove that the person who signed the contract or the power of attorney (as the case may be) was in fact the general director of the company, and the latter extract may prove that the same general director was in place at the time of performance and hence refute the argument that, when performing the contract, the general director did not know that it was void and thus is not estopped from arguing its invalidity. The extracts also prove the company's registered address.

3. Obtain certified copies of the contract at the moment of its execution or shortly thereafter. These will allow you to have the copies of the arbitration agreement required for enforcement under the New York Convention, and to produce apostilled copies of the contract in the Russian courts when necessary. Original documents should not be filed with the Russian courts or law-enforcement agencies, as they may not be returned.

4. Obtain certified copies of corporate approvals of the contract issued by the board of directors and the general assembly of shareholders of the Russian counterparty if there is any risk that the transaction in question could be characterized as a major or interested party transaction. Such documents are more easily obtainable just after the contract is signed (for example by way of a condition precedent to the contract's entry into force) than once a conflict has arisen.

5. Obtain any available documents likely to prove that the contract in question was concluded at a fair market price and at arm's length and thus did not harm the interests of the Russian counterparty or its shareholders (again, for the purpose of countering indirect claims).

Once the dispute has arisen:

6. Obtain and keep receipts of delivery of the notice of arbitration and other key documents to the Russian counterparty by courier or registered post. Although many institutional rules provide that the request for arbitration should be sent to the respondent by the institution and not by the claimant, it may be advisable to send the request to the respondent anyway, in order to obtain such evidence (alternatively, institutions may be persuaded to provide certified copies of delivery receipts). Although arbitration rules generally allow communications to be sent to the last known address of the respondent, duplicates should also be sent to the respondent's registered address, given that such service is required under the procedural rules of the *Arbitrazh* courts (the latter have been known to apply the same rule, wrongly, at the enforcement stage). Claimants should also obtain an extract from the Joint State Register of Companies of the Russian Federation at the time the relevant document is served, indicating the respondent's up-to-date registered address. Sometimes it may also make sense to deliver communications personally through a Russian lawyer, who may be able to obtain from the defendant company a stamped copy of each communication showing the date on which the defendant company received it.

7. Always call for an original, or certified copy, of the power of attorney granted by the Russian company to its lawyer, and make sure that the terms of such power of attorney are wide enough to cover all the actions carried out by the lawyer (including receipt of relevant communications) and that the power of attorney is valid for the entire duration of the proceedings. If the arbitral tribunal does not take the initiative of asking to see a valid power of attorney from the Russian company during the arbitration, the non-Russian party should seek to persuade it to do so. The non-Russian party may then produce the power of attorney at the enforcement stage to prove that (for example) the Russian party's lawyer was authorized to represent it at the hearing.

8. If law other than Russian law has been chosen as the law governing the contract in the circumstances described in point 1 above, and if the specific facts of the dispute would allow Russian law to be applied without affecting the result, consider accepting that 'mandatory' rules of Russian law should be applied in place of the chosen law or concurrently with it (making sure that such application of Russian law is clearly stated in the award). Arbitrators should similarly be aware that failure to apply Russian 'mandatory' rules (even if the claimant invites them not to apply such rules and even if they consider that such rules are not, in fact, mandatory) may have negative consequences for the claimant at the enforcement stage.

9. Formulate the relief requested in such a way as to generate the least possible hostility in the mind of the Russian court of enforcement. In particular, avoid any relief that seems to impinge on the 'exclusive jurisdiction' of the *Arbitrazh* courts set out in Article 248 of the *Arbitrazh* Procedural Code. For example, avoid any declaration as to ownership of real property (as opposed to an order for payment of damages for failure to transfer ownership). Also avoid requesting an order for damages calculated on the basis of the claimant's contribution to the share capital of a Russian joint venture (such an order might be construed as amounting to an order for the liquidation of the joint venture), as opposed to loss of value of the claimant's investment caused by the defendant's actions. Orders for specific performance should always be accompanied by a monetary award in the event that the defendant fails to comply by a certain date, as Russian bailiffs lack the practical ability or incentive to enforce orders for specific performance alone. As far as pecuniary damages are concerned, Russian courts are reluctant to enforce awards of liquidated damages far in excess of the actual loss, so it may be appropriate, in certain circumstances, for claimants to reduce their claims in order to increase the chances of successful enforcement. All amounts awarded should be clearly indicated in the dispositive part of the award, and any formulae for calculating interest should be easily understandable to Russian judges and bailiffs. If the claimant has a Russian affiliate, the award should provide an option for collection of the damages in rubles (this may simplify enforcement and help avoid problems with Russian currency control bodies).

10. If you know your Russian counterparty has initiated or will initiate an indirect claim in the Russian courts, consider applying for an anti-suit injunction, either from the arbitral tribunal or the courts at the seat of the arbitration, against both the defendant and the shareholder/claimant in the Russian proceedings. Clearly, an injunction issued against a non-signatory to the arbitration agreement may be difficult to obtain. However, in some circumstances tribunals and national courts may be prepared to pierce the corporate veil. Court injunctions can be a real deterrent to Russian companies, given the potential criminal sanctions that can be applied to directors personally. Finally, in the event that an indirect claim is brought, it may well be worth fighting it in the Russian courts rather than choosing simply to ignore it.