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Russia

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A. Legislation and rules

1 November 2017 marked the end of the transition period of the new arbitration laws passed in December 2015 and taking effect on 1 September 2016.³ As of that date, only those arbitral institutions that met the requirements of the new arbitration law⁴ are able to administer arbitrations in Russia. There are four such institutions at present: the Arbitration Court at the RSPP⁵ and the Institute of Modern Arbitration⁶, both of which obtained the “license,” in addition to the International Commercial Arbitration Court and the Maritime Arbitration Commission. Other Russian arbitration courts are not entitled to administer arbitrations in Russia, and awards issued in Russia in proceedings administered by such Russian institutions without the “license” are considered to be issued in breach of the statutory arbitration procedure.⁷

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³ Federal Law No 382-FZ: “On arbitration (arbitration proceedings) in the Russian Federation,” dated 29 December 2015 (the “Law on Domestic Arbitration”) and the accompanying Federal Law N 409-FZ amending relevant statutory acts, including Law N 5338-1, adopted on 7 July 1993 (the “Law on ICA”).

⁴ The new arbitration law stipulated that arbitral institutions need to obtain a special “license” from the Russian government in order to be able to administer arbitrations in Russia. Exception was made for the International Commercial Arbitration Court and the Maritime Arbitration Commission at the Russian Chamber of Commerce and Industry (the “ICAC” and the “MAC” respectively).

⁵ Arbitration Court at the Russian Union of Industrialists and Entrepreneurs, <https://arbitration-rspp.ru>.

⁶ <http://modernarbitration.ru/en>.

⁷ Article 52(15) of the Law on Domestic Arbitration.

Arbitrations with the place of arbitration in Russia, administered by foreign arbitration institutions, would still be valid, but will be considered for the purpose of Russian arbitration laws to be ad hoc arbitrations. In a practical sense, it means that the parties to such arbitrations would not enjoy certain benefits provided by Russian law to institutional arbitrations (like waiving in advance the opportunity to challenge an award on jurisdiction or on the merits). Also, unless the parties agree on storing the arbitration case file, including an arbitral award, with a licensed arbitral institution in Russia, arbitrators in such arbitrations would need to deposit it with a local Russian court that is competent to enforce the award.⁸

B. Cases

B.1 Enforcement of an award that is res judicata in relation to the enforced award is contrary to national public policy⁹

The case concerns enforcement in Russia of a DIS award made in 2015¹⁰ in a dispute between the parties out of an exclusive distribution agreement (the “Agreement”) made in 2001. The Agreement provided Lugana with an exclusive right to sell in South-East Asia the reed relays manufactured by the Plant and precluded the Plant from entering into contracts for the sale of reed relays on the specified territory, with a penalty imposed for such breach in Article 5.3, constituting 50% of the price of contracts that were signed bypassing the Agreement. A penalty in the amount of USD 939,447¹¹ was awarded under the 2015 Award and became subject of the enforcement proceedings. Courts of two levels enforced the 2015

⁸ See Article 39 of the Law on Domestic Arbitration.

⁹ *Lugana Handelsgesellschaft mbH i.L (“Lugana”) v. Ryazan Metallic and Ceramic Equipment Plant (“Plant”)*, case A54-3603/2016, case file at: <http://kad.arbitr.ru/Card/984201b5-27f5-4699-8908-efcca7e4e5d4>.

¹⁰ The DIS award was made on 6 February 2015 in case DIS-SV-CB-303/13.

¹¹ According to the 2015 Award, the Plant was ordered to pay Lugana USD 939,447.96 with 5% interest above the base rate thereon, starting from 30 September 2004, and half of the DIS administrative fee of EUR 6,309.90.



Award.¹² At cassation level, the Plant first argued that the same Agreement had already been the subject of an earlier DIS arbitration that led to the issuance of three arbitral awards¹³ enforced in 2010.¹⁴ The 2005 award of 11 August 2005 was, as argued by the Plant, *res judicata* in relation to the 2015 Award. The Supreme Court at the second cassation review upheld these arguments and refused to enforce the 2015 Award for violation of public policy. The Supreme Court held that such enforcement would violate the principle of legality of a judicial act and disrupt legal certainty, established by a foreign arbitral award duly enforced in Russia.¹⁵ Both legality and legal certainty are part of Russia's public policy according to the Court.

Without seeing the awards themselves only limited reasoning is possible as to the *res judicata* effect of the 2005 Award in respect of the 2015 Award. On the one hand, both awards were issued between the same parties on the same grounds (the Agreement) and with the same subject matter (a breach of the exclusivity granted to Lugana). On the other hand, the 2015 tribunal ruled that the validity of the 2005 Award did not preclude the new proceedings, finding that the previous tribunal did not intend to and in fact had not ruled on claims 3b) and

¹² Ruling of Ryazan region Arbitrazh Court dated 14 October 2016 in case A54-3603/2016; Resolution of the Arbitrazh Court of Central Circuit dated 14 March 2017 in case A54-3603/2016.

¹³ The first award dated 11 August 2005 in case No DIS-SV-B-454/04 ordered the recovery from the Plant of USD 463,317.63 in penalties, with 8% interest thereon above the base rate as from 23 January 2003, and ordered the Plant to supply 500,000 reed relays at a particular price. The second award dated 14 October 2005 in case No DIS-SV-B-454/04 ruled on partial costs, including the arbitration fee and legal costs of EUR 81,652.05 paid by Lugana and interest starting from 15 September 2005. The third arbitral award dated 27 December 2005 in case No DIS-SV-B-454/04 ruled on final costs whereby the further arbitration fee and legal costs of EUR 57,408.71 and interest starting from 6 December 2005 were awarded to Lugana. The enforcement of the 2005 Awards was discussed in *The Baker & McKenzie International Arbitration Yearbook 2010-2011*, pages 336-337.

¹⁴ See Resolution of the Supreme Arbitrazh Court dated 2 February 2010 No 13211/09 in case A54-3028/2008, case file at:<http://kad.arbitr.ru/Card/8e390bd0-ba6d-4a52-8f2d-7c96d8b1fca5>.

¹⁵ Resolution of the Supreme Court dated 27 September 2017.

3c) of the 2004 arbitration claim.¹⁶ Should this be the case, then it could be argued that the previous award did not have a *res judicata* effect in respect of the issues left undecided. For example, the 2005 Award could have dealt with either penalties for breach of other provisions of the Agreement or penalties for breach of exclusivity in respect of those contracts that were known to Lugana at the time. This sounds probable, given that one of the claims in the 2005 Award of 11 August was disclosure by the Plant of all contracts entered into in breach of the Agreement. However, one thing remains unclear: why were the undecided claims transferred to another tribunal instead of being decided by the same arbitrators? We may be able to see these arguments voiced by Lugana, should the case be transferred to the Presidium of the Supreme Court for supervisory review on the merits.

B.2 The possibility of submitting a domestic Russian dispute to foreign arbitration¹⁷

The case deals with the enforcement in Russia of a foreign arbitral award¹⁸ issued in Singapore in a dispute between Russian parties out of a legal services agreement. The Arbitrazh Court of Moscow refused enforcement on the grounds of a public policy violation, finding that the parties had no connection to a foreign jurisdiction.¹⁹ After a cassation court sent the case back for retrial, the same first level court dismissed the claims on the grounds that the award issued at an address in Moscow was a domestic award and that enforcement of a domestic award using the procedure for enforcement of a foreign award contradicted Russian public policy.²⁰ Thus, the court failed to resolve the issue of whether purely domestic disputes could be

¹⁶ See Resolution of the Supreme Court dated 27 September 2017, pages 9-10.

¹⁷ *Common Legal Property LLC v. Techno-Art LLC*, case A40-219464/16-52-430, case file at: <http://kad.arbitr.ru/Card/b9fce500-8a18-42a6-a333-42608356008a>

¹⁸ An award issued by Russia-Singapore Arbitration (<http://rsa.sg/>) dated 30 August 2016 in case No RSA-5/16.

¹⁹ Decision of Arbitrazh Court of Moscow dated 20 January 2017.

²⁰ Decision of Arbitrazh Court of Moscow dated 5 May 2017, upheld by Resolution of the Arbitrazh Court of Moscow Circuit dated 19 July 2017. The Supreme Court on 13 November 2017 refused to consider the cassation appeal on the merits.



arbitrated abroad. Moreover, it disregarded one of the fundamentals of arbitration, namely, that arbitration seat is a legal fiction and has no connection with the actual location of the tribunal resolving a case. The court also added one more ground for refusal to enforce, namely, that the award violated the principles of arbitration proceedings such as independence and impartiality. The court found that the claimant in this case was engaged in business of obtaining writs of execution for awards of the Moscow Court of Commercial Arbitration. The sole arbitrator that issued the award in the case, Mr. Kravtsov, was Chair of Russia-Singapore Arbitration and the Moscow Court of Commercial Arbitration and was affiliated with the claimant.

B.3 Enforcement refused due to multiple violations of public policy²¹

In this case, a losing party successfully argued numerous violations of public policy that either led to the review of the award on the merits (and not a correct one at that) or represented the erroneous application of the law.²²

SPIG filed for enforcement of an SCC award dated 1 September 2016 in case No V 2015/099, which was refused by the Arbitrazh Court of Moscow.²³ The Court agreed with Promcontroller (the respondent) that the SCC award breached public policy due to the following: (1) the tribunal applied the CISG;²⁴ (2) the tribunal released SPIG of guarantee obligations under the contract; (3) OGK-2, a customer under the contract, would not be able to claim damages due to the termination of the contract; (4) the tribunal awarded lost profits, which represented unjust enrichment of SPIG; (5) SPIG changed both the

²¹ *SPIG s.p.a. (“SPIG”) v. Promcontroller Production Company CJSC* (“Promcontroller”), case A40-230545/2016, case file at: <https://kad.arbitr.ru/Card/71e6b9a3-25b9-4db3-97f9-c2010d120b79>.

²² For example, arguments regarding the breach of the arbitration agreement of the parties in relation to the applicable procedural law and seat.

²³ Decision of Arbitrazh Court of Moscow dated 16 March 2017 in case A40-230545/16-29-2261.

²⁴ 1980 UN Convention on Contracts for the International Sale of Goods.

grounds and subject matter of the claim by first claiming 10% of the price that remained outstanding and then damages for failure to perform the contract; (6) the SCC applied Swedish law on arbitration, thus breaching the parties' arbitration agreement; (7) the proceedings were conducted in Moscow despite the seat being in Stockholm; (8) the award was issued by two arbitrators despite the parties having agreed to three in the arbitration agreement. Although SPIG's objections to the alleged violations, as set down in the trial court's decision, were reasonable and founded in law²⁵ the cassation court upheld the decision.²⁶ The Supreme Court refused to consider the case on the merits.²⁷ This highly controversial case demonstrates that Russian courts continue to interpret the public policy objection broadly.

B.4 The tribunal's failure to examine the underlying contract as the major transaction is a violation of public policy²⁸

This case of enforcing an award by the ICAC of Ukraine represents another example of a broad interpretation by Russian courts of the public policy objection. This time, the courts found that an LLC with RUB 10,000 charter capital was the sole founder and the director of the debtor and that the ICAC of Ukraine failed to examine whether the lease agreement in dispute had been approved as a major transaction under the Russian LLC Law. This, in the courts' view, amounted to a violation of public policy and justified refusal to enforce the award.²⁹

²⁵ For example, Promcontroller argued that the CISG was not applicable as the parties chose "Russian legislation" and not "Russian law" to govern the contract. The tribunal found that Promcontroller agreed to the application of CISG by failure to raise a timely objection to such application and citing the CISG rules itself.

²⁶ Resolution of Arbitrazh Court of Moscow Circuit dated 24 May 2017.

²⁷ Ruling of the Supreme Court dated 2 October 2017.

²⁸ *Ukrainian Chemical Products ChAO (Ukraine) v. Titan Investments LLC (Russia)*, case A40-77427/2017, case file at: <https://kad.arbitr.ru/Card/d557bb83-9e78-4efd-bbdb-1912c3cec528>.

²⁹ See Decision of Arbitrazh Court of Moscow dated 20 July 2017, upheld by Resolution of the Arbitrazh Court of Moscow Circuit dated 27 October 2017.



B.5 An individual's right of recourse to court and the possibility to limit this right of one's own free will by making use of ADR methods forms part of public policy³⁰

KNIC filed for enforcement of 12 awards issued in disputes under various reinsurance agreements under English law between KNIC and MSK Insurance Group OJSC³¹ in ad hoc arbitrations seated in London. The courts of two levels granted enforcement.³² In particular, the cassation court dismissed a number of the debtor's arguments on breach of public policy³³ and held that the assessment of whether the enforcement of an award is contrary to public policy could not lead to the award's review on the merits.³⁴ The cassation court accepted as evidence an affidavit of an English-qualified lawyer clarifying the issues of executing reinsurance agreements, procedural aspects of arbitral proceedings, use of electronic means in notifying parties, and requirements to the form of the arbitration agreement (a written form recorded by any means). However, the Supreme Court overturned the decisions in the course of the second tier cassation review and ordered a retrial of the case.³⁵ The Supreme Court ruled that an original or a duly certified copy of an arbitration agreement be submitted to confirm whether a party has freely waived its right to have the dispute adjudicated by a state court. According to the Supreme Court, "*an individual's right to access to court and the possibility to limit this*

³⁰ *Korea National Insurance Corporation ("KNIC") v. VTB Insurance LLC ("VTB Insurance")*, case A40-60583/2016, case file at: <https://kad.arbitr.ru/Card/d9ad5ac7-f5a6-4565-99af-63a2993a4e4d>.

³¹ VTB Insurance is a successor of MSK Insurance Group OJSC.

³² Decision of Arbitrazh Court of Moscow dated 18 November 2016 in case A40-60583/2016; Resolution of Arbitrazh Court of Moscow Circuit dated 19 January 2017 in case A40-60583/2016.

³³ This included the lack of acceptance of reinsurance agreements, their failure to prove obligations to pay the reinsurance indemnity, lapse of limitation periods on the date of arbitration proceedings, failure to use electronic correspondence due to lack of specific provisions in the contract to that effect, as well as of email addresses for official exchange of correspondence.

³⁴ The Arbitrazh Court of Moscow Circuit relied on the Information Letter of the Supreme Arbitrazh Court No156 dated 26 February 2013.

³⁵ Supreme Court Ruling dated 4 September 2017.

right of one's own free will by making use of alternative dispute resolution methods, including international commercial arbitration, forms part of ... public policy."

B.6 Lack of funds to pay an arbitration fee does not render an arbitration clause incapable of being performed³⁶

Redius-T filed a claim with an arbitrazh court for the recovery of money and interest under a supply contract. The first level court terminated the proceedings without prejudice due to a valid SCC arbitration clause and dismissed the arguments that the applicant's lack of funds to pay the arbitration fee resulted in a breach of its right of access to courts.³⁷ The appeal court found the applicant proved inability to arbitrate due to a lack of funds (confirmed by a tax filing), and the SCC's confirmation of terminating proceedings without payment of the fee, and sent the case to retrial.³⁸ This decision was overturned by both cassation instances. The courts found no confirmation of the arbitration clause being null and void, inoperable or incapable of being performed. The courts added that the fact of financial difficulties of a party which is a commercial organization cannot *per se* serve as grounds for a state court to decide the case on the merits where there is a valid arbitration clause.³⁹ The Supreme Court refused to consider the supervisory appeal on the merits.⁴⁰

³⁶ *Redius-T LLC v. GSE Krass LLC*, case A56-13914/2016, case file at: <https://kad.arbitr.ru/Card/b6ce2c26-2bad-46ce-aaf7-def0eb942605>.

³⁷ Decision of the Arbitrazh Court of St. Petersburg and Leningrad region dated 6 June 2016.

³⁸ Resolution of the 8th Arbitrazh Court of Appeal dated 25 August 2016.

³⁹ Resolution of Arbitrazh Court of North-Western Circuit dated 3 November 2016; Resolution of the Supreme Court dated 12 July 2017.

⁴⁰ Ruling of the Supreme Court dated 11 December 2017.



B.7 Disputes out of contracts entered into to implement a state program are non-arbitrable⁴¹

The case demonstrates an increasing willingness by courts to consider as non-arbitrable those disputes that involve budget funds or other public elements. The dispute arose out of a contract for construction works that was signed within the framework of implementing a state program for urban planning in Moscow for 2012–2018 in accordance with provisions of the federal law on procurement of goods, works and services by state legal entities. An arbitration court awarded *Mosteplosetjstroy* RUB 5.2 million. Lower courts enforced the award, whereas the Supreme Court overturned the decisions and found grounds to submit the case for cassation review on the merits. It stayed proceedings in the case and requested a constitutional court to rule whether disputes in connection with performance of contracts by state companies and other entities whose activities are governed by relevant federal law are arbitrable.

C. Funding in international arbitration

There is no specific regulation of third-party funding in Russia.

At the same time, in a number of recent cases the party opposing an arbitration clause used a defense of lack of funds to finance arbitration proceedings. We have already discussed one of the cases above, where courts ruled that financial difficulties of a party that had agreed to arbitration cannot affect the validity of the arbitration clause.

However, the issue becomes more complex once bankruptcy proceedings are involved. In another case, a party seeking relief with a state court, despite an arbitration clause in the contract, claimed it was unable to pay the arbitration fee due to bankruptcy proceedings and having creditors' claims included in the register of around RUB 22

⁴¹ *Mosteplosetjstroy JSC v. Moinzhprojekt JSC*, case A40-165680/2016, case file at: <http://kad.arbitr.ru/Kad/Card?number=%D0%9040-165680%2F2016>.

billion.⁴² The court refused to uphold the defense saying that mere financial difficulties do not render an arbitration clause inoperable or oblige a state court to resolve the case on the merits. But this time, the court went beyond this finding and held that “*a mere fact of a claimant being in bankruptcy does not release it from complying with the dispute resolution procedure envisaged by the agreement by the parties. A party may abandon an arbitration clause only where a claimant in fact has no funds to cover arbitration costs, except for instances where such claimant is abusing its rights.*”⁴³ The court analyzed a bankruptcy manager’s report and the results of bankruptcy and held that the amount of assets and monetary funds in the debtor’s accounts as well as its monthly income enabled it to pay the USD 3,000 registration fee and request the other payments be postponed. Then, the court calculated that the debtor would have funds available after selling its assets and paying its security creditors, as per the provisions of the bankruptcy law, to cover arbitration costs. The court of appeal upheld the judgment.⁴⁴ Cassation appeal is pending.

⁴² Case A81-4101/2016, case file at: <http://kad.arbitr.ru/Card/318fdb55-93d8-4a8e-8e0a-eea882c6c018>.

⁴³ Decision of the Arbitrazh Court of Yamalo-Nenetsky area dated 23 August 2017.

⁴⁴ Decision of the 8th Arbitrazh Court of Appeal dated 26 October 2017.