RUSSIAN FEDERATION

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A. LEGISLATION, TRENDS AND TENDENCIES

There have been no recent changes in the Russian legislation on arbitration.

However, in 2011, the Russian Constitutional Court rendered a decision of importance for arbitration which finally resolved the issue of the "arbitrability" of disputes concerning registered rights to immovable property.

The legislation of the Russian Federation does not contain a prohibition against referring civil law disputes concerning immovable property to courts of arbitration;[3] it in fact directly provides for such a possibility.[4] Nevertheless, over the course of

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3 As has been established in the legal doctrine, exceptions to the arbitrability of cases should be made only by federal law. *See* Makovsky A.L., Karabelnikov B.R. "Arbitrability of Disputes: the Russian Approach," // International Commercial Arbitration. 2004. N 3. p. 21.

4 *See* part 1 Art. 25, Federal Law No. 102-FZ of 16 July 1998 "On Mortgage (Pledge of Property):" 1. Unless otherwise stipulated in the Federal Law or this Article, a registration entry on mortgage is expunged … based on a declaration by the holder of a mortgage, a joint declaration of a pledgor and a pledgee, a declaration of a pledgor with presentation of … a decision of a court, arbitrazh court or arbitration court to terminate the mortgage."

the last several years, the Supreme Arbitrazh Court and Supreme Court have quite consistently adhered to the point of view that such disputes are not subject to arbitration.

The Supreme Arbitrazh Court's logic boiled down to the following:[5]

- The decision of an arbitration court on the ownership rights to immovable property forms the basis for registering ownership rights to that property.
- Legal relations connected to registration of ownership rights (i.e., legal relations between the state registration authority registering rights to immovable property and the right holder) are of a matter of public law.
- The arbitration court is not entitled to take a decision compelling the state registration authority to register immovable property in the name of the party to the arbitration proceedings, since public law matters (such as the registration of real estate rights) cannot be submitted to arbitration.

The Supreme Arbitrazh Court stated that an arbitration court was also not entitled to levy execution on pledged immovable property, as those disputes likewise fall under the exclusive jurisdiction of state courts.[6]

In accordance with that logic, Arbitrazh courts in the Russian Federation declared that matters dealing with the termination or change of the term of long-term lease agreements for immovable property are also not subject to arbitration, since any lease of

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5 Clause 27, Information Letter of the Presidium of the Supreme Arbitrazh Court of the RF of 22 December 2005 No. 96 "Survey of the practice of arbitrazh courts' consideration of cases to recognize and enforce awards of foreign courts, to challenge awards of arbitration courts and to issue writs of execution for enforcement of awards from arbitration courts."

6 *Ibid*. clause 28.

immovable property for longer than one year is subject to registration with state authorities.[7]

Without disputing the Supreme Arbitrazh Court's view that an arbitral tribunal cannot compel a state registration authority to register immovable property, one is hard-pressed not to notice an error in the logic of the highest judiciary. Indeed, legal relations between the parties to the sale of immovable property, and those between the state registration authority and the parties are different. And the fact that the arbitral tribunal is not entitled to resolve administrative disputes with a state registration authority related to a refusal to register rights to the property does not mean that it is not entitled to resolve disputes relating to ownership rights between the parties of a sale transaction.

It is interesting to note that the Supreme Court also excluded arbitrability of disputes related to immovable property, providing an even less persuasive justification. The Supreme Court stated that an arbitral award could not be grounds for registering rights to immovable property, since it did not possess that quality of decisions passed by courts of general jurisdiction, i.e., the "legal force of a court decision."[8]

Apparently realizing the weakness in the logic behind prohibiting the referral of immovable property disputes to arbitration, the Supreme Arbitrazh Court approached the Constitutional Court of the Russian Federation in 2010 for clarification as to whether arbitral tribunals could take a decision to levy execution on property under a mortgage agreement.

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7 Resolution of Moscow Region Federal Arbitrazh Court, 3 September 2007, No. KG-A40/8370-07.

8 Reply to Question 2 on civil cases in Survey, appr. by Resolution of Presidium of RF Supreme Court of 7 November 2007. The text of the Survey was not officially published.

On 26 May 2011, the Constitutional Court handed down a Resolution, ruling that disputes over registered rights to immovable property could be subject to arbitration,[9] stating as follows: ". . . if the decision of a court of arbitration adopted upon the results of considering a dispute concerning immovable property establishes the rights to said property, the registering body must perform actions for their state registration . . ."

Accordingly, the Supreme Arbitrazh Court likewise stated:[10] "At present, federal legislation does not establish the exclusive jurisdiction of state courts to consider disputes concerning immovable property; courts of arbitration are entitled to resolve disputes on levy of execution on immovable property pledged under a mortgage agreement."

B. CASES

B.1 *Stena RoRo AB (Sweden) v. Baltiysky Zavod OJSC (RF)*

Under two shipbuilding contracts Baltiysky Zavod OJSC ("Baltiysky") was to design and build two ROPAKS-class vessels for Stena RoRo AB ("Stena".) On the same day the parties signed an option agreement for two additional vessels with the same characteristics, which option was to become

[9] Resolution of the RF Constitutional Court of 26 May 2011, in a case to inspect the constitutionality of the provisions of Article 11.1 of the RF Civil Code, Art. 1.2 of the Federal Law "On Courts of Arbitration in the Russian Federation," Art. 28 of the Federal Law "On state registration of rights to and transactions involving immovable property," Art. 33.1 and 51 of the Federal Law "On mortgage (pledge of property)" in connection with a request by the RF Supreme Arbitrazh Court.

[10] Resolution of the Presidium of the RF Supreme Arbitrazh Court of 27 September 2011 in case No. 530/10.

effective once the shipbuilding contracts came into force. All contracts were governed by Swedish law, and contained an SCC arbitration clause.

The shipbuilding contracts were made conditional on their approval by the board of directors of the Baltiysky and Stena. Stena considered the approval obtained, and the shipbuilding contracts entered into force. In 2005, Baltiysky changed owners, and a year later, the new owners of the factory, deeming the contracts a loss, refused to fulfill them.[11]

Citing the seller's improper performance of the contracts, as well as of the option agreement, Stena initiated arbitration under the SCC Rules against Baltiysky for recovery of EUR 145,563,862 in losses.

During the arbitration, Baltiysky mainly relied on a rather formal argument that the contracts had not entered into force because they had not been approved by the board of directors of the opposing party—Stena. Although Stena had produced a letter to Baltiysky confirming that its board of directors had approved those transactions, Baltiysky stated that this was not sufficient, because the decision should have been executed in the form of minutes, which was not presented to Baltiysky.[12]

The arbitral tribunal rejected that argument, stating that Baltiysky had accepted the letter about the Stena board decision without any criticisms, and failed to request a copy of minutes. What's more, additional agreements were signed and both sides acted as if the contracts were already in force. In particular, Baltiysky issued a press release on the conclusion of the contracts, took part in meetings and held negotiations on related

11 http://pravo.ru/news/view/63281/

12 Circumstances of the case are reconstructed in Resolution of the Presidium of the RF Supreme Arbitrazh Court in case no. 9899/09 of 13 September 2011.

contracts, proposed raising the price for the vessels, and only on 23 June 2006 did it inform Stena of its contention that there was no legal obligation to fulfill the contracts.

The arbitrators stated that formal approval was neither a requirement of the law nor of the contracts, and the lack of formal approval was significant only as a matter of proof regarding whether approval was in fact given.

In its final decision, on 24 September 2008, the arbitral tribunal awarded Stena EUR 20,000,000 in losses caused by the non-fulfillment of the contracts, arbitration costs, and expenses incurred in connection with the arbitration and interest.

It should be noted that this amount was in fact accepted by Baltiysky during the arbitration, which stated in its submission that "if the arbitral tribunal considers the shipbuilding contracts and option agreement as having come into force and being subject to fulfillment according to their conditions, the factory agrees to pay a fine of 20 million euro, i.e., in an amount equal to the 'estimated' losses in accordance with Article XI.B 2(b) of the shipbuilding contracts, including the option agreement."

Nonetheless, Baltiysky submitted an application to the Svea Court of Appeal to have the award set aside, citing the fact that there was no valid contract between the parties, and therefore also no arbitration agreement, since Stena's board of directors had not ratified the transaction within the stated deadline.

Meanwhile, Stena initiated enforcement proceedings in Russia.

On 20 February 2009, the Arbitrazh Court of St. Petersburg and the Leningrad Region refused enforcement of the SCC award, finding that it was against the public order of the Russian Federation, and "was made in a dispute not falling within the scope of the arbitration clause in the non-concluded contracts of which it is a component part." The court stated that the

arbitration clause was contained in contracts that had not entered into force, as the decision of the Swedish company's board of directors to approve the transactions was not formalized by minutes. The fact that no official minutes were passed to Baltiysky constitutes a breach of a fundamental principle of Russian law, based on recognition of the equality of participants in civil law relations as laid down in Article 1 of the Civil Code.

In refusing to enforce the SCC award, the court also stated that enforcement of the award against Baltiysky—a strategic enterprise with a special management right on the part of the state—might cause it to go bankrupt. This would result in damage to the sovereignty and security of the state and would contravene the public order of the Russian Federation.[13]

On 24 April 2009, the Federal Arbitrazh Court of the North-Western Circuit upheld the decision of the trial court.[14] The cassation court, however, disagreed with the conclusions of the trial court that the arbitration agreement was not concluded and that the Factory's bankruptcy would result in damaging the state sovereignty and thus was contrary to the public order. The cassation court's reasoning was expressed as follows:[15]

> The public order of the Russian Federation . . . shall be understood to refer to the fundamentals of law and order in the Russian Federation.
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> In turn, the fundamentals of law and order in the Russian Federation comprise, in addition to the foundations of morality, the major religious teachings, main economic and

[13] Ruling of the Arbitrazh Court of St. Petersburg and Leningrad Region in case no. A56-60007/2008.

[14] Resolution of FAS SZO [Federal Arbitrazh Court of the North-Western Circuit], 24 April 2009, in case no. A56-60007/2008.

[15] Resolution of FAS SZO, 24 April 2009, in case no. A56-60007/2008.

> cultural traditions making up Russian civil society, and the basic principles of Russian law.
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> The basic principles of Russian law, in particular, include the principal fundamentals of civil law.
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> Likewise, the basic principles of Russian civil law include the main rules for assigning responsibility for non-performance of obligations, specifying in particular that responsibility for causing damage (tort liability) arises only in case of the guilt of the debtor (Article 1064 of the RF CC), and also that a party not performing (or improperly performing) an obligation when engaging in business activity bears liability if it does not prove that due performance was impossible as a result of force majeure (Article 401, RF CC)). . .
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> Due to the fact that there are no contractual obligations between [*Stena RoRo AB*] and [*Baltiysky Zavod OJSC*] to construct and deliver ROPAKS-class vessels, the latter may not be charged with liability in the form of compensation for losses due to their non-performance. . .

The supervisory proceedings initiated by *Stena RoRo AB* were stayed pending the appeal of *Baltiysky Zavod OJSC* in the Swedish state courts.[16]

On 20 May 2010, the Svea Court of Appeal upheld the SCC award, stating in its final judgment that *Stena RoRo AB* had presented sufficiently convincing proof to the effect that its board of directors had ratified the transaction within the stated deadline.

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[16] Judicial act not yet published. Information from the SAC RF's official site can be found at http://www.arbitr.ru/vas/presidium/nadzor/25447.html.

Thereafter, the Supreme Arbitrazh Court overturned the decision of the lower courts and passed a decision to enforce the foreign arbitral award.[17] The Supreme Arbitrazh Court did not agree with the conclusions of the Federal Arbitrazh Court of the North-Western Circuit that the absence of minutes of the company's board of directors on approval of the contracts ran contrary to the public order of the Russian Federation due to a breach in the principles of freedom of contract and equality of its parties. The Supreme Arbitrazh Court held that the question of whether the Swedish company's board of directors followed the procedure for approving the contracts had already been resolved by the arbitral tribunal, applying Swedish law as agreed by the parties, and the courts were not entitled to revisit this matter on its merits, and certainly not by applying Russian law. Furthermore, this same issue had been resolved already by the Svea Court of Appeal. The Supreme Arbitrazh Court stated:[18]

> Under the legislation of the Russian Federation, [*Baltiysky Zavod OJSC*] should have formalized, and actually did formalize in minutes, the consent of its board of directors to the conclusion of the contracts. However, it does not follow from this circumstance that the Swedish company, due to the factory's actions as conditioned by Russian law, and the necessity of observing in civil-law relations the principle of equality of the parties, acquires the counter-obligation to submit documents evidencing the similar consent of its own board of directors specifically in the form of minutes.
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> The rules set forth by Russian legislation on documenting decisions by the management bodies of Russian legal entities

[17] Resolution of the Presidium of the RF Supreme Arbitrazh Court in case no. 9899/09 of 13 September 2011.

[18] Resolution of the Presidium of the RF Supreme Arbitrazh Court in case no. 9899/09 of 13 September 2011.

> do not extend to Swedish companies. By entering into contracts with the terms of their being subordinate to Swedish substantive law, [*Baltiysky Zavod OJSC*] assumed risks connected with the fact that the relevant legal order might contain provisions differing from the norms of Russian law regulating analogous relations . . .
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> …
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> Determination of the losses was done by the arbitral tribunal based on Swedish law applicable to relations between the parties, taking into account the conditions of the contracts and option agreement specifying the possibility of recovering losses in a 'fixed,' previously agreed amount . . . the arbitrators awarded these losses as liquidated damages . . . By its legal nature, they are similar to the concept of a penalty used in Russian civil law . . .
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> Thus, both the penalty and the losses are specified by civil legislation and form part of the legal system of the Russian Federation. Therefore, *ipso facto*, application of these measures of liability cannot contravene the RF public order.

However, the story does not end here. The respondent also tried to employ certain "guerilla tactics" well known in Russia: a derivative action.

On 16 March 2010, the Arbitrazh Court of St. Petersburg and the Leningrad Region granted the claim of the minority shareholders in *Baltiysky Zavod OJSC* and rendered the shipbuilding contracts invalid. It also declared the option agreement invalid on the basis that it had "not been concluded."

The court of appeal agreed that under Russian law a claim seeking to declare a transaction null and void may be filed by

any interested parties, including a company's shareholder.[19] The court of cassation affirmed.[20]

The courts found abuse of right on the part of Stena, in particular, because of the fact that it and the Swedish company knew that Baltiysky signed contracts that both were unfavorable for it. Baltiysky also signed a "consciously unperformable contract, "since it undertook to issue a guarantee from the Savings Bank of the RF which would be regulated by Swedish law (which is impossible under Russian law) and without indicating a specific term of its validity (which also contradicts mandatory requirements of Russian law regarding guarantee)."

On 13 September 2011, the Supreme Arbitrazh Court overturned the decisions of lower courts and issued a judgment on the merits of the case, rejecting the stated claims and saying:[21]

> . . . the courts' conclusion about the impossibility of a Russian bank to give a guarantee in accordance with Swedish law contravenes the norms of Russian law, specifically Articles 1186 and 1217 of the Civil Code, as well as the provisions of Article 27 of the ICC Uniform Rules on Demand Guarantees, according to which in a guarantee or counter-guarantee, only if otherwise is not set forth, the governing law is the law of the location of the guarantor or instructing party (depending on the case) or, if the guarantor or instructing party has several locations, then

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19 *See* Resolution of 13th Arbitrazh Court of Appeals, 7 July 2010, case no. A56-6656/2010.

20 Resolution of Federal Arbitrazh Court of North-Western Circuit, 25 October 2010, case no. A56-6656/2010.

21 Resolution of the Presidium of the RF Supreme Arbitrazh Court in case no. 1795/11 of 13 September 2011.

> the law of the location of that branch office which issued the guarantee or counter-guarantee.
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> …
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> The other circumstances to which the courts referred as evidencing that [*Baltiysky Zavod OJSC*] performance of obligations under the contracts was knowingly impossible, in particular, the impossibility of the receiving by [*Baltiysky Zavod OJSC*] an advance payment in the absence of a bank guarantee, in and of themselves did not hinder the performance of obligations by [*Baltiysky Zavod OJSC*], as the works should have been done by using [*Baltiysky Zavod OJSC*] own funds.
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> Furthermore, the courts' conclusion about abuse of its rights by *Stena RoRo* when entering into the disputed transactions is not supported by Russian law . . .
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> …

Both cases were reviewed by the RF Supreme Arbitrazh Court on the same day, though the cases were not officially consolidated.

B.2 *Tabellion Limited* (the Republic of Cyprus) *v. A. G. Ischuk* (Russian Federation)

This case likewise furnishes an example of an attempt to use the guerilla tactics of "a derivative action," when a transaction which was the subject of international arbitration proceedings is declared invalid not upon the claim of a minority shareholder, but at the claim of a spouse of the individual. Here is the history of the case.

On 6 December 2007, the company Tabellion Limited ("Tabellion") and the company Federalevel Holdings Limited ("Federalevel") concluded a sale-purchase contract for shares

and an option to sell. Performance of obligations by Federalevel was guaranteed by an RF citizen, A.G. Ischuk.[22]

Due to the failure of Federalevel and Ischuk to perform their obligations, Tabellion initiated proceedings under the LCIA Rules, which granted Tabellion's claims against Federalevel and Ischuk. In particular, Ischuk was obliged to pay (or ensure payment by Federalevel) of USD 43,426,229.51.

On 6 June 2011, the Samara Region Arbitrazh Court refused to enforce the LCIA award as being contrary to the Russian Federation public order. The trial court held that the fact that A.G. Ischuk's wife, I.A. Ischuk, was not a party to the LCIA arbitration was a breach of the public order. This was because enforcement of the award would involve the property belonging to her as Mr. Ischuk's wife in accordance with the provisions of Russian Federation Family Code (the "RF FC").

However, on 9 August 2011, the Federal Arbitrazh Court of the Povolzhsky Circuit overturned the trial court's decision, stating as follows:

> . . . under the provisions of Article 35.2 of the RF FC, when one spouse concludes a transaction to dispose of the spouses' common property, it is presumed that he or she is acting with the consent of the other spouse. A transaction completed by one of the spouses for disposal of the spouses' common property may be declared invalid by a court due to the absence of the other spouse's consent only at his or her demand and only in cases when it is proven that the other party to the transaction knew or should have known of the other spouse's lack of consent to the completion of that transaction.

[22] Case described in Resolution of Federal Arbitrazh Court of Povolzhsky Circuit, 9 August 2011, case no. A55-27265/2010.

The Supreme Arbitrazh Court shared the cassation court's view.[23]

B.3 *Ciments Francais (France) v. Holding Company Sibirsky Cement OJSC (Russia) and İstanbul Çimento Yatırımları Anonim Şirketi (Turkey)*

This case is an example of the successful application of guerilla tactics in international arbitration.

On 7 December 2010, an ICC arbitral tribunal with its seat in Istanbul, Turkey, issued a partial award in case No. 1624/GZ initiated by Ciments Francais against Holding Company Sibirsky Cement OJSC (hereinafter "Sibirsky Cement") and İstanbul Çimento Yatırımları Anonim Şirketi *(*hereinafter "İstanbul Çimento Yatırımları").

The arbitral tribunal in its partial award found that Ciments Francais duly exercised its right to terminate a share sale-purchase agreement concluded on 26 March 2008 between Sibirsky Cement, Ciments Francais and İstanbul Çimento Yatırımları (the "SPA"), and further, that it had the right to withhold the amount of the original payment of EUR 50 million paid by Sibirsky Cement. The arbitral tribunal also stated that the partial arbitral award was to be enforced immediately.

After the arbitral tribunal issued the partial award, it was set aside by a Turkish court of the first instance pursuant to an application by Sibirsky Cement.

The grounds for setting aside the award were the following:

(a) The Turkish court agreed with Sibirsky Cement's argument that the arbitral award was not issued within the set deadline.

[23] Ruling to refuse to refer a case to the Presidium of the RF Supreme Arbitrazh Court of 12 December 2011 in case no. SAC-15654/11.

This circumstance constitutes independent grounds for setting aside the arbitral award in accordance with Article 15.1.c of Law of Turkey No. 4686 "On International Arbitration" (hereinafter "Law No. 4686").[24]

(b) The Turkish court also concluded that the arbitral tribunal had exceeded its authority. This was based on the fact that the ICC arbitral tribunal did not consider the debtor's argument on the termination of the SPA in accordance with the principle of good faith. An arbitrator's (or tribunal's) exceeding of authority is a ground for setting aside an arbitral award under Law No. 4686.[25]

(c) The Turkish court found that the arbitral award contravened public order, as it provided for it to have immediate effect, and also due to the fact that the parties to the arbitration agreement waived the right to submit an application to set aside the award.

Further, in anticipation of the ICC partial arbitral award, FPS Sibconcorde LLC (a minority shareholder in Sibirsky Cement) submitted a claim to the Kemerovo Region Arbitrazh Court for invalidation of the SPA. The SPA, being a major transaction under the Russian Federation joint stock companies law, required the approval of the General Shareholders' Meeting of Sibirsky Cement. The decision of this meeting approving the SPA had been declared invalid in earlier court proceedings initiated by Sibconcorde LLC on the grounds that Sibconcorde LLC did not receive all information on that transaction, was not notified of the date of the general meeting, and did not take part

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[24] This standard states "the award was not issued during the arbitration term."

[25] Art. 15.1.e of the Law says: "an arbitrator or arbitral tribunal handed down an award in a matter beyond the limits of the arbitration agreement, or did not hand down an award concerning all demands, or exceeded its authority."

in that meeting.[26] Ciments Francais was not a party to those proceedings.

On 13 August 2010, the Kemerovo Region Arbitrazh Court, disregarding the ICC arbitration clause in the SPA, granted the claim of the minority shareholder to declare the SPA invalid and ordered Ciments Francais to return EUR 50 million to Sibirsky Cement OJSC.[27] Ciments Francais argued that the courts should have stayed proceedings in this case due to the arbitration clause in the SPA. However, the court dismissed this argument on the basis that the claimant was not a party to the SPA and was thus not bound by it.

On 20 July 2011, the Kemerovo Region Arbitrazh Court,[28] which considered an application to recognize the foreign arbitral award, rejected the argument that it contravened public order because it was contrary to the Russian trial court's decision [the decision for invalidation of the SPA]. This was because this decision was disputed in a pending appellate procedure and as of the date of consideration had not entered into legal force (Arbitrazh Procedure Code provides that the trial court's decision does not enter into force while an appeal is pending).

The Kemerovo Region Arbitrazh Court, analyzing the provisions of the European Convention on International Commercial Arbitration, to which Russia is a party, concluded that setting aside the award in the country where it had been issued entailed a refusal to recognize and enforce the arbitral award only when it was set aside on one of the grounds indicated in subclauses (a)-

[26] Decision of Kemerovo Region Arbitrazh Court dd. 04 February 2009 in case no. A27-16841/2008-3.

[27] Decision of Kemerovo Region Arbitrazh Court dd. 13 August 2010, in case no. A27-4626/2009.

[28] Ruling of Kemerovo Region Arbitrazh Court, 20 July 2011, case no. A27-781/2011.

(d) of Article IX(1) of the European Convention.[29] As the grounds upon which the Turkish court set aside the award were not specified by the European Convention, the fact that it was set aside in Turkey did not entail refusal to recognize the arbitral award in the Russian Federation. Also, the Turkish court decision was being appealed in Turkey and thus was not final.

However, on 5 December 2011, a higher court overturned the lower court's ruling based on the violation of the Russian Federation public order. The court held that the law regarding the mandatory nature of the Russian state courts' decisions and their execution represent the elements of the Russian Federation public order. As the decision of the Kemerovo Region Arbitrazh Court whereby the SPA had been declared invalid, had entered into force the court concluded that: "Therefore, the recognition and enforcement of an arbitral award issued based on an invalid transaction will result in the existence on the territory of the Russian Federation of court acts of equal legal force with mutually exclusive conclusions, and will contradict the principles of the mandatory nature of Russian courts' decisions, which represent an inseparable part of the Russian Federation public order."[30]

Furthermore, the cassation court, referred to the fact that the arbitral award was set aside by a Turkish court, which in the cassation court's view was grounds for refusal to recognize the

[29] Article IX(1) of the European Convention states: "The setting aside in a Contracting State of an arbitral award covered by this Convention shall only constitute a ground for the refusal of recognition or enforcement in another Contracting State where such setting aside took place in a State in which, or under the law of which, the award has been made and for one of the following reasons …". That said, clause 2 of this Article IX states that clause 1 of Article IX takes priority over the respective provisions of the New York Convention.

[30] Resolution of the Federal Arbitrazh Court of West-Siberian Circuit dd. 05 December 2011 in case no. A27-781/2011.

foreign award based on Article V(1)(e) of the New York Convention as well as Subclause 1 of Article 36.1 of RF Law No. 5338-1 "On International Commercial Arbitration" dated 7 July 1993.

Thus, the cassation court in essence ignored the provisions of the European Convention, which take priority over the provisions of the New York Convention, as well as over the national legislation of the Russian Federation by virtue of the constitutional principle of the priority of international law over national law. It did so without explaining the reasoning for such a position.

C. PUBLIC POLICY IN INTERNATIONAL ARBITRATION

C.1 Scenarios of Reliance on Public Policy

In Russia public policy considerations can be invoked in any proceeding where the court considers, either on its own initiative or at the request of a party, that an arbitration agreement or arbitral award is contrary to a public policy of the Russian Federation.

In particular, these issues can be raised by a party or *ex officio* by court in proceedings where:

(a) one of the parties to the arbitration agreement, disregarding it, files a claim on a merit of the dispute covered by the arbitration agreement, before a Russian state court; or

(b) one of the parties files a claim to invalidate the arbitration agreement; or

(c) a party to arbitration files an application to set aside the arbitral award issued in Russia; or

(d) recognition and enforcement of a foreign arbitral award is sought.[31]

C.2 Modes and Limitations of Reliance on Public Policy

There are no time limits in Russian law for invoking the public policy defense.

From that perspective, it does not really matter whether the same issue was raised before the tribunal and how the tribunal dealt with this issue.

It is also worth noting that Russian law does not distinguish between international public policy and public policy of the Russian Federation, referring only to the latter. Similarly, Russian courts also mainly refer to the public policy of Russia in their decisions.

Russia is a party to the 1961 European Convention on International Commercial Arbitration ("the European Convention"). The European Convention limits the application of clause V(1)(e) of the New York Convention through its clause IX, which provides that the annulment of the award at the place of arbitration can lead to the refusal in recognition of the award only if the award has been annulled on the grounds specified in clause IX of the European Convention.

Violation of public policy is not listed among the grounds in clause IX of the European Convention, however, as was highlighted above in the summary of the *Ciments Francais v. Holding Company Sibirsky Cement OJSC (Russia) and İstanbul Çimento Yatırımları Anonim Şirketi (Turkey)* case, the Russian courts did not apply the European Convention according to its

[31] Sub-par. 2 Article 36(1) of the RF Law "On International Commercial Arbitration."

language and its spirit. It is therefore possible that Russian courts would adopt the same approach with regard to public policy issues.

C.3 Rules that Constitute "Public Policy"

Public order is referred to in Article 1193 of the Civil Code of the Russian Federation as "fundamentals of the legal order of the Russian Federation." However, there is no legal definition of public order in the Russian Federation Law "On International Commercial Arbitration" which leaves space for a broad interpretation of the concept by Russian state courts.

In its Ruling of 25 September 1998, the Supreme Court stated that when the court based its decision on Russian law the decision could not be reversed as being contrary to public order, as application of Russian law provisions could not be considered as breach of Russian public policy:

> RF public order is understood to mean the fundamentals of the social order of the Russian state. Invoking a public policy provision is only possible in those individual cases where the application of foreign law could bring about a result impermissible from the viewpoint of Russian legal conscience.[32]

This definition is still widely used by Russian courts.[33]

The Supreme Arbitrazh Court in one of its cases[34] stipulated that a foreign arbitral award violates the Russian Federation public order when its enforcement leads to actions that are:

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32 RF Supreme Court Ruling of 25 September 1998 in case no. 5-G98-60.

33 Resolution of the Federal Arbitrazh Court of the North-Western Circuit of 28 December 2009 in case no. A21-802/2009.

34 RF SAC Ruling No.13452/07 of 6 December 2007.

- expressly prohibited by the law;
- damaging the sovereignty or security of the state;
- affecting the interests of major social groups;
- incompatible with the principles of economic, political and legal system of the state;
- affecting the constitutional rights and freedoms of citizens; or
- contradicting the major civil law principles such as equality of the parties, inviolability of property, freedom of contract.

According to the Supreme Arbitrazh Court, the improper or unjustified assessment by the arbitral tribunal of the circumstances and facts of the case, as well as its failure to properly apply civil law rules regulating specific legal relations of the parties arising out of their contract, cannot be considered a breach of public policy.

In practice, there is no threshold for application of public policy arguments and in the past Russian courts usually applied it broadly. In recent years, however, the Supreme Arbitrazh Court, considering particular cases, employs a pretty narrow view as to what constitutes public policy. At the same time, lower courts often do not follow the same approach.