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DEVELOPMENTS IN RUSSIAN ARBITRATION LAW

by Vladimir Khvalei and Ekaterina Solomatina,
Baker & McKenzie, Moscow

A. LEGISLATION, TRENDS AND TENDENCIES

The Law On International Commercial Arbitration, enacted on 7 July 1993, is based on (indeed almost identical to) the UNCITRAL Model Law provisions. Russia is also a party to the European Convention on International Commercial Arbitration of 1961 and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958 (New York Convention). Domestic arbitration is governed by the 2002 Law on Arbitration Courts in the Russian Federation and it is also based on the principles of the UNCITRAL Model Law. No amendments were made to the abovementioned laws in 2008.

B. CASES

Details are given below of recent judgments handed down by the Russian courts in cases related to arbitration involving foreign companies. There are also references to cases which do not involve foreign companies, because it is safe to assume that the Russian courts would adopt a similar approach to cases whether or not a foreign company is a party. These decisions below are mainly the judgments of the first level arbitrazh[1] courts and the third level courts

[1] The Russian word arbitrazh is not related to arbitration but originates from an old Soviet tradition, whereby disputes between state enterprises were heard before the so-called 'State Arbitrazh.' In the USSR, it was assumed that under a planned economy no real disputes could arise between socialist enterprises (since all enterprises ultimately had the same owner), and any differences which did arise could be settled by an intermediary, the State Arbitrazh, which was a quasi-judicial governmental institution (in fact it was part of the government).

(the Federal Arbitrazh Court or so called "cassation courts"). This is because any application to set aside an arbitral award or to issue a writ of execution in respect of awards made by domestic arbitration courts, as well as applications for recognition and enforcement of foreign arbitral awards, must be filed in the first level court, while an appeal against the judgment of a court of first instance in such cases is to be filed directly in the third level court, *i.e.*, with the Federal Arbitrazh Court.

B.1 An Agreement to Arbitrate is Not Concluded if the Parties did not Agree as to What Particular Arbitration Institution Shall Consider the Dispute and Only One Party is Entitled to Select an Arbitral Institution at its Discretion

On 24 August 2007, OOO Rosich and businessman Turlakov, Victor Ivanovich, entered into an agreement according to which any disputes arising under or in connection with such agreement shall be resolved by an arbitration institution to be determined at the claimant's discretion, provided that the institution is within the confines of the Tomsk Oblast.

Turlakov having failed to perform duly under the agreement, OOO Rosich filed a claim under the Rules of the Arbitration Court at the Limited Liability Company "Yuristy Sibiri" (Siberian Lawyers) (hereinafter referred to as the "Siberian Lawyers Ltd. Arbitration Court"), which on 15 January 2008 rendered an award in favor of OOO Rosich for 5,625 rubles of lost profit, 4,500 rubles of arbitration fees and expenses, and 30,000 rubles of legal fees.

On 28 February 2008, the Arbitrazh Court of the Tomsk Oblast refused an application for the issuance of a writ of execution for enforcement of the arbitral award. The Federal Arbitrazh Court of the Western Siberian Region confirmed the judgment of the court of first instance.

OOO Rosich appealed to the Supreme Arbitrazh Court of the Russian Federation, insisting that the aforesaid decisions be re-

versed, but the Supreme Arbitrazh Court of the Russian Federation saw no reasons for so doing.[2]

In particular, the Supreme Arbitrazh Court of the Russian Federation pointed out the following:

> The wording used by the parties expressly admits the claimant's sole discretion in selecting any arbitration institution within the confines of the Tomsk Oblast to review a specific dispute arising out of the agreement concluded by and between the parties. However, a dispute may only be referred to arbitration if the parties to the dispute have entered into an agreement in respect thereof on the basis of which it can be determined what particular arbitration tribunal the dispute shall be referred to.

This conclusion confirms the earlier view of the Supreme Arbitrazh Court of the Russian Federation according to which an agreement to arbitrate may not be deemed concluded if the parties did not specify the arbitration institution or procedure under which an *ad hoc* tribunal is to be appointed.

For example, in its Resolution No. 5278/95 of 27 February 1996, the Supreme Arbitrazh Court of the Russian Federation said, in part: "According to Articles 2 and 8 of the Provisional Regulation on the Court of Arbitration for Resolution of Economic Disputes in the Russian Federation,[3] an agreement to refer disputes to arbitration must incorporate some information on what particular arbitration institution shall be entrusted with arbitration or that information making it evident that the parties will establish an *ad hoc* arbitral tribunal to review a specific dispute pursuant to the applicable procedure."[4]

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[2] Ruling No. 8711/08, dated 28 August 2008, by the Supreme Arbitrazh Court of the Russian Federation.

[3] Approved by the RF Supreme Soviet's Resolution No. 3115-1 of 24 June 1992 "On Approval of the Provisional Regulation on the Court of Arbitration for Resolution of Economic Disputes" — author's note.

[4] Apropos, neither Article 2 ("Arbitration Courts"), nor Article 8 ("Decision by Arbitral Tribunal on the Possibility of Reviewing a Dispute") contained any provisions making it possible to arrive at the conclusion that an agreement to refer a dispute to arbi-

In its letter of 16 February 1998, the Supreme Arbitrazh Court of the Russian Federation said that the arbitration clause in the contract, according to which all differences arising out of the contract shall be referred to the "Paris Institute," would be deemed unenforceable.[5]

Meanwhile, it would be worthwhile to mention here the dispute between the state-owned company "Optika No. 1" and OOO Expotrans referred to the Court of Arbitration for Resolution of Economic Disputes under the Chamber of Commerce and Industry of the Ulyanovsk Oblast. The contract concluded by and between the aforesaid entities did provide for referral of disputes to the Private Court of Arbitration of the Ulyanovsk Oblast. In this case, however, the Supreme Arbitrazh Court of the Russian Federation saw no reasons for setting aside the arbitral award.[6] In the opinion of the supreme judicial instance, in the aforesaid case, "an agreement to arbitrate as concluded by the parties did provide that relevant disputes shall be referred to the Arbitration Court of the Ulyanovsk Oblast and, consequently, did not expressly give right to only one of the parties sole discretion in selecting an arbitration institution for reviewing such disputes."[7]

B.2 Disputes Regarding Extension of the Lease of Real Estate Property are not Arbitrable

As reported in the 2007 edition of this yearbook, disputes related to registrable rights over immovable property are not arbitrable. In 2008, the arbitrazh courts decided several cases which illustrate this principle, including cases involving long terms lease agreements.

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tration shall specify the permanent arbitration institution or that the dispute will be considered by *ad hoc* tribunal.

5 *See* Section 13 of News Letter No. 29, dated 16 February 1998, by the Presidium of the Supreme Arbitrazh Court of the Russian Federation "Review of Arbitrazh Court Practice to Resolve Disputes in Cases Involving Foreign Persons."

6 Resolution No. 1120/07, dated 24 July 2007, by Presidium of the Supreme Arbitrazh Court of the Russian Federation.

7 Determination No. 8711/08, dated 28 August 2008, of the Supreme Arbitrazh Court of the Russian Federation.

In 1997, Kalinka-Stockmann as tenant entered into a 10-year agreement for lease of premises in the business complex "Smolensky Passazh" in downtown Moscow. The lease provided for the tenant's right to extend the lease term for another 10-year period on the terms and conditions applicable within the past five years of the effective term of the original lease. In 2007, the landlord refused to extend the lease on the agreed-upon terms and conditions and was therefore sued by Kalinka-Stockmann which referred the dispute to the International Commercial Arbitration Court under the Chamber of Commerce and Industry of the Russian Federation ("ICAC") in accordance with the arbitration clause contained in the lease.

On 29 April 2008, the tribunal acting under ICAC Rules rendered an award in favor of the claimant. The award supported the claimant's right to extend the lease term for another 10-year period on the earlier agreed terms and conditions. The arbitration court obliged the respondent to enter into an extension by executing and registering an addendum to the original lease of 1997. On 14 August 2008, the Arbitrazh Court of the City of Moscow set aside the ICAC award. One of the reasons for this decision was the fact that the dispute could not be the subject matter of arbitration. On 13 October 2008, the Federal Arbitrazh Court of the Moscow Region upheld the position of the Moscow City Arbitrazh Court.[8]

The cassation court said that by recognizing Kalinka-Stockmann's right to have the lease extended and by compelling the respondent to extend the effective term thereof and enter into and register an addendum to the original lease, the ICAC had effectively extended the contractual relationship under the lease on definite terms and conditions for ten years. The original lease agreement, as well as the 2000 addendum thereto, had been duly registered, so an agreement to alter the lease subject to state registration should also be subject to state registration.

The legal relationships associated with the state registration of rights are of a public nature and questions regarding rights to immovable property fall within the exclusive competence of state courts.

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[8] Ruling No. KG-A40/9294-08-1,2 of 13 October 2008 by the Federal Arbitrazh Court of the Moscow Region.

Therefore, the conclusion by the court of first instance to set aside the arbitral award rendered in respect to a non-arbitrable dispute was, in the opinion of the Federal Arbitrazh Court of the Moscow Region, correctly decided.

A similar conclusion regarding non-arbitrability of the subject matter of the dispute was drawn by the Arbitrazh Court of the City of Moscow and the Federal Arbitrazh Court of the Moscow Region when they set aside an award rendered by the ICAC on 29 April 2008 with respect to Kalinka-Stockmann's claim against another landlord attempting to compel the latter to extend a 2005 lease agreement for a new term on the same terms and conditions.[9]

B.3 Litigant Failing to Make an Objection to the Jurisdiction of the State Court With Reference to the Arbitration Clause Prior to the First Hearing on the Merits Waives its Right to Arbitration

OOO Ponate ARD sued Hochtief Aktiengesellschaft in the Arbitrazh Court of the City of Moscow despite the arbitration clause in the agreement.[10] In the court of first instance, the respondent did not object to the jurisdiction of the Arbitrazh Court of the City of Moscow to consider the dispute and the court proceeded with examination of the case on its merits, refusing to satisfy the claims in its judgment of 12 March 2007. On 10 April 2007, the cassation court reversed the judgment of the trial court, ordering that the case be re-examined.

During re-examination of the case by the Arbitrazh Court of the City of Moscow, the respondent filed an objection to the case being tried by the arbitrazh court, referring to the arbitration clause in the agreement. On 24 December 2007, the court granted the motion, referring to Article 148, Clause 5, of the Code of Arbitrazh Procedure of the Russian Federation (reflecting Article II(3) of the New York Convention) in accordance with which an arbitrazh court shall leave a statement of claim unheard upon establishing that:

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[9] Ruling No. KG-A40/9254-08 of 13 October 2008 by the Federal Arbitrazh Court of the Moscow Region.

[10] Ruling No. KG-A40/3239-08 of 4 May 2008 by the Federal Arbitrazh Court of the Moscow Region.

- there is an agreement between the litigants to submit the dispute to a private arbitration and
- if either litigant objects to the jurisdiction of the state court on or before its submission on the merits of the case,

unless the court determines that the agreement is null and void, has become inoperative or incapable of being performed.

On 31 January 2008, an appellate court reversed the aforesaid decision because of incorrect use of procedural law norms and ordered that the case be retried by the court of first instance. On 4 May 2008, the Federal Arbitrazh Court of the Moscow Region confirmed the correctness of the appellate court's position, stating the following:

> Filing a motion to refer the dispute to arbitration... if made when the cassation court already has reversed the decisions [of the lower courts] in the case and ordered retrial of the case, shall not entail those consequences provided under Article 148, Clause 5, of the Code of Arbitrazh Procedure of the Russian Federation, because the arbitration clause in such case shall be deemed terminated.

B.4 Party Failing to Object to the Arbitral Tribunal's Jurisdiction in a Timely Manner Waives Its Right to File Any Such Objection in the Future

On 10 January 2008, the Court of Arbitration under the Moscow Chamber of Commerce and Industry made an award on Case No. A-2007/7 in favor of Berlin-Chemie that had sued Vedant Ltd. and OOO Intercare.

The losing party (OOO Intercare) applied to the Arbitrazh Court of the City of Moscow for setting aside the award, arguing that there had been no arbitration agreement between the parties. While explaining its position, the applicant told the court that the general director executing the contract with an arbitration clause therein on the applicant's behalf no longer held the position of general director at the time of the execution of the contract with the result that the arbitration clause was not binding.

On 19 May 2008, the Arbitrazh Court of the City of Moscow found the above arguments to be reasonable and set aside the award. On

31 July 2008, the Federal Arbitrazh Court of the Moscow Region reversed the decision of the Arbitrazh Court of the City of Moscow.[11]

In substantiation of its decision, the cassation court explained as follows:

> [I]n accordance with Article 4 of the RF Law 'On International Commercial Arbitration,' a party who knows that any provision of this Law from which the parties may derogate or any requirement under the arbitration agreement has not been complied with and yet proceeds with the arbitration without stating its objection to such non-compliance without undue delay or, if a time limit is provided therefor, within such period of time, shall be deemed to have waived its right to object.
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> According to Article 16, Paragraph 2, of the aforesaid Law, a plea that the arbitral tribunal does not have jurisdiction shall be raised not later than the submission of the statement of defence. A party is not precluded from raising such a plea by the fact that it has appointed, or participated in the appointment of, an arbitrator. A plea that the arbitral tribunal is exceeding the scope of its authority shall be raised as soon as the matter alleged to be beyond the scope of its authority is raised during the arbitral proceedings. The arbitral tribunal may, in either case, admit a later plea if it considers the delay justified.
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> Meanwhile, OOO Intercare took part in the arbitration proceedings of the Court of Arbitration under the Chamber of Commerce and Industry, submitted its statement of defense and provided supporting evidence.

The cassation instance also pointed out that no statement had been made to the effect that the arbitral tribunal had no jurisdiction, so that the Court of Arbitration under the Moscow Chamber of Commerce and Industry had no reason to decide that it did not have such jurisdiction.

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[11] Resolution No. KG-A40/6468-08, dated 31 July 2008, of the Federal Arbitrazh Court of the Moscow Region.

B.5 An Interim Arbitral Award on Lack of Jurisdiction is not Subject to Challenge. A Judgment by the Arbitrazh Court in Which the Interim Award on Jurisdiction was Challenged is Subject to Appeal for Cassational or Supervisory Review

IManagement Services Ltd. filed a claim against Cukorova Holding Anonim Sirketi with the Court of Arbitration under the Chamber of Commerce and Industry of the Moscow Oblast. On 14 November 2006, the tribunal acting under the rules of the aforesaid institution rendered an award saying that it had no jurisdiction. The claimant applied to the Arbitrazh Court of the City of Moscow for an order setting aside the arbitral award. Having considered the application on its merits, the Arbitrazh Court of the City of Moscow refused to allow the claim and so did the cassation court, both courts referring to the lack of any grounds for setting aside the award as provided under Article 233 of the Code of Arbitrazh Procedure of the Russian Federation.[12]

The Presidium of the Supreme Arbitrazh Court of the Russian Federation reversed both these judicial decisions, saying that Article 235, Part 1, of the Code of Arbitrazh Procedure of the Russian Federation provided for a litigant's right to apply to an arbitrazh court for setting aside the positive arbitral interim award on its jurisdiction.[13] But an interim arbitral award regarding the lack of jurisdiction may not be set aside as such. This is why the arbitrazh court of first instance, rather than considering the substance of application should have terminated the proceeding in the case.

Based on the foregoing, the Supreme Arbitrazh Court rendered a judgment to terminate the proceeding in the case on the basis

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[12] Article 233 of the Code of Arbitrazh Procedure of the Russian Federation provides, in part: "A party to an arbitration proceeding may file an application with an arbitrazh court requesting that it set aside the arbitral interim award on its jurisdiction if an international agreement to which the Russian Federation is party or federal law so provides."

[13] Resolution No. 2384/08, dated 27 May 2008, of the Presidium of the Supreme Arbitrazh Court of the Russian Federation.

of Article 150 of the Code of Arbitrazh Procedure of the Russian Federation.[14]

B.6 Where the Arbitral Tribunal Decides the Dispute by Rendering an "Award" Rather than Issuing an "Order," this Shall Entail Reversal of Such Decision

The RF Law "On International Commercial Arbitration" makes a distinction between two kinds of decisions or acts that may be rendered by an arbitral tribunal, namely, "award" and "order."[15]

An "award" implies a decision taken in relation to the substance of the dispute. The award shall state the reasons upon which it is based, explain whether the relief sought by the claimant has been granted or rejected, indicate the amount of the arbitration fees and costs and allocation of it between the parties. Also, the award shall state its date and place of arbitration.[16]

An "order" is understood to mean a decision of procedural issues. The arbitral tribunal shall issue an order for the termination of arbitral proceedings when:

- the claimant withdraws his claim;
- the parties agree on the termination of the proceedings;
- the arbitral tribunal finds that the continuation of the proceedings has for any other reason become unnecessary or impossible.[17]

The ICAC Rules also draw the line between an "award" and an "order."[18]

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[14] In accordance with this provision, the arbitrazh court should terminate the proceeding in the case, particularly if the case is not subject to trial by an arbitrazh court.

[15] *See*, for example, Article 32, Paragraph 1, of RF Law No. 5338-I "On International Commercial Arbitration," dated 7 July 1993.

[16] Article 31, Paragraphs 1 and 2, of the Law "On International Commercial Arbitration."

[17] Article 32, Paragraph 2, of the RF Law "On International Commercial Arbitration," dated 7 July 1993.

[18] § 45 of the Rules of the ICAC under the Chamber of Commerce and Industry of the Russian Federation: "If no final award is made in a case, the arbitral proceedings shall be terminated by an order."

On 8 February 2008, a panel of arbitrators acting pursuant to the ICAC Rules made an award for termination of the proceedings in Case No. 18/2007 re: OAO Gazprom vs. AOOT Moldovagaz, ruling that the claimant had failed duly to comply with pre-arbitration dispute settlement procedures.[19] On 24 July 2008, the Arbitrazh Court of the City of Moscow satisfied OAO Gazprom's request to have the ICAC award set aside.

On 18 September 2008, the Federal Arbitrazh Court of the Moscow Region upheld the first level court judgment, indicating, among other things, that the arbitral tribunal should have made its decision in the form of an order rather than by rendering an award. In addition, the "award" made by the arbitral tribunal failed to explain whether relief sought had been granted or rejected, an omission that violated the provisions of Article 31, Paragraph 2, of the RF Law "On International Commercial Arbitration."[20]

B.7 Public Policy

The argument that an arbitral award contradicts public policy is the one quite often resorted to by the party seeking to set aside the award or objecting to recognition and enforcement of a foreign arbitral award. Several cases were tried by arbitrazh courts in 2008 in which the questions of public policy were raised during the proceedings.

OAO Sudpromkomplekt (Russia) vs. ZORYA-MASHPROEKT (Ukraine)

In this case, OAO Sudpromkomplekt argued that an ICAC award ordering OAO Sudpromkomplekt to pay an amount of losses worth 339,840.00 US Dollars contradicts public policy. It was argued

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[19] § 45, Clause 2 (B), of the Rules of the ICAC under the Chamber of Commerce and Industry of the Russian Federation provides that arbitration proceedings shall be terminated "when the arbitral tribunal finds that continuation of the proceedings has become unnecessary or impossible for any reasons, in particular, in the absence of prerequisites required for the case to be arbitrated and decided on its merits, such as where, owing to the claimant's inaction, the case makes no progress for more than six months."

[20] Resolution No. KG-A40/8586-08, dated 18 September 2008, of the Federal Arbitrazh Court of the Moscow Region.

that the damages amounted to penalties imposed on the claimant in accordance with the Ukrainian Law "On the Foreign Currency Payments" for failure to transfer in a timely manner hard currency revenues accruing from export transactions, such failure occurring due to late payments by the company for services rendered thereto.

The Supreme Arbitrazh Court held[21] that the order for payment of these losses was entirely consistent with the requirements of Article 15, Clauses 1 and 2, of the Civil Code of the Russian Federation, which says that a person whose right has been violated may demand full compensation for the losses caused to him, including those costs which the person whose right has been violated incurred or must incur in order to reinstate the right that has been violated (actual damage).

The judgment of the court contained the following comments regarding public policy:

> An award rendered by an international arbitration tribunal may be deemed as contradictory to public policy of the Russian Federation if, as a result of enforcement thereof, there will be committed any acts either expressly prohibited by law or inflicting damage on the sovereignty and security of the State, affecting the interests of large social groups, being inconsistent with the principles of building up the economic, political and legal systems of states, affecting the constitutional rights and freedoms of citizens, or contradicting the basic principles of civil legislation, such as the quality of litigants, inviolability of property, freedom of contracts.
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> The argument referring to violation of public policy may only be accepted to the extent that foreign law applies, but if the award was rendered on the basis of the provisions of Russian law, then violation of public policy of the Russian Federation may only result from failure to comply with the basic principles of procedural legislation.

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[21] Determination No. 13452/07, dated 6 December 2007, by the Supreme Arbitrazh Court of the Russian Federation.

> Meanwhile, neither the assessment by the international arbitral tribunal of evidence available in the case, which is inappropriate in the opinion of the company, nor the tribunal's unreasonable and incorrect use of certain provisions of civil legislation regulating specific legal relationships arising out of the contract between the parties in the course of engagement by the parties in entrepreneurial activities, shall be deemed to constitute grounds for setting aside of the award rendered by the ICAC under the Chamber of Commerce and Industry of the Russian Federation for reasons of violating public policy.

Czechoslovak Commercial Bank vs. OAO Kamchatgazprom

In other proceedings, the arguments about non-compliance with public policy were made by OAO Kamchatgazprom and rejected by the Arbitrazh Court of the Kamchatka Oblast in a decision on recognition and enforcement of the award made by the Court of Arbitration under the Rules of the Economic Chamber of the Czech Republic and the Agrarian Chamber of the Czech Republic.

OAO Kamchatgazprom challenged the decision. The arguments inherent in the appeal centered around allegations of breach of public policy of the Russian Federation, because the arbitral tribunal had:

- failed to take into account the fact that the claimant was not guilty of failure to perform its obligations under the loan agreement;
- ordered compound interest; and
- failed to take into account the fact that the bank received insurance compensation payments stipulated under an insurance policy covering the risk of failure to repay the loan.

The Federal Arbitrazh Court of the Far Eastern Region turned down the arguments of the cassation appeal, saying that recovery of debts and interest under the loan agreement was consistent with the normal business customs of the Russian Federation and the provisions of Russian civil law.[22]

[22] Ruling No. F03-A24/07-1/6043, dated 12 March 2008, by the Federal Arbitrazh Court of the Far Eastern Region.

In addition, recovery of interest as a late payment charge to the debtor of loan repayments, including the principal amount of the loan and interest accruing thereon as a charge for use of the loan, was held to be perfectly consistent with the provisions of Russian legislation and the principle of commensurability of liability for the consequences of failure duly to perform one's obligations.

Moreover, the obligation of the debtor to the creditor is, consistent with the provisions of Russian legislation, notwithstanding that the creditor receives insurance proceeds for the same debt.

Kalinka-Stockmann vs. ZAO AKB Mosstroyeconombank

In this case the ICAC panel of arbitrators made an award on recognition of the claimant's right to extend the lease agreement concluded with the respondent in 2005 for a new ten-year period on the earlier negotiated terms and conditions. And yet it was evident from the text of the judicial act[23] that the surviving lease rate substantially differed from the prevailing market rate.[24]

One of the arguments used by the respondent in the arbitration was that the award on the extension of the lease agreement would be unenforceable, as it would contradict the provisions of Article 40 of the Russian Federation's Tax Code.[25] Article 40 of the Tax Code incorporating the rules for determining the prices of goods and services for the purposes of taxation holds the taxpayers liable for selling goods or services at a price which is more than 20% (above or) below the prevailing market price.

So in the event that the sale price of goods sold, work performed or services rendered deviates from the prevailing market price by more than 20%, the tax authorities will be entitled to decide to impose additional taxes and penalties calculated on the difference between transaction price and market price.

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[23] Ruling No. KG-A40/9254-08, dated 13 October 2008, by the Federal Arbitrazh Court of the Moscow Region.

[24] Five to seven times, according to different estimates.

[25] As far as can be seen from the text of this judicial act, this is because the ICAC award in question is not publicly available.

Thus, the respondent argued that the ICAC award would be unenforceable, as it would virtually force ZAO AKB Mosstroyeconombank into committing unlawful acts (selling services at a price which would be more than 20% below the prevailing market price).[26]

In its decision[27] the Federal Arbitrazh Court of the Moscow Region acknowledged that the ICAC award in relation to the matter in question was discriminatory in substance, as it compelled ZAO AKB Mosstroyeconombank to lease premises to the claimant for a period of ten years on terms knowingly inconsistent with the objectives of entrepreneurial activities, something that, for its part, violated Article 34 of the Constitution of the Russian Federation.[28]

The cassation court made the following comments concerning public policy in the context of the issue:

> [T]he discharge of the landlord's duties arising out of the award made by the ICAC under the Chamber of Commerce and Industry of the Russian Federation, notably, conclusion of a lease agreement at a price substantially below the market price, will compel the landlord to commit a tax offence and assume the burden of resulting unfavorable property consequences provided under Article 40 of the Russian Federation's Tax Code, which is inadmissible. No arbitral award shall prescribe committing offences, for any such offence will infringe on public law and order.

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[26] It was presumably for that reason that the ICAC award mentioned the fact that the right to extend the lease agreement for a new term may be exercised by the claimant under the condition of compliance with mandatory provisions of legislation in effect in the Russian Federation, including the provisions of Article 40 of the Russian Federation's Tax Code.

[27] Resolution No. KG-A40/9254-08, dated 13 October 2008, by the Federal Arbitrazh Court of the Moscow Region.

[28] Article 34 of the Russian Federation's Constitution provides that everybody shall have the right to free and unimpeded use of one's capabilities and property for the purposes of entrepreneurial activities or any other activities not prohibited by law.

In accordance with the RF Constitutional Court's Resolution No. 2-P,[29] dated 02.05.2007, the general legal principle of legal distinctness implies the stability of legal regulation and enforceability of judicial decisions. This panel of judges is of the opinion that the award rendered by the ICAC under the Chamber of Commerce and Industry of the Russian Federation, by infringing on the aforesaid principle, actually infringes on public law and order in the Russian Federation. Having recognized the claimant's right to extend the earlier concluded lease agreement, subject to the provisions of Article 40 of the Russian Federation's Tax Code, the arbitral tribunal nevertheless failed to offer a method for exercising such right or explain the terms and conditions on which such right shall be exercised and the timing for exercising such right, thus making its award virtually unenforceable and inconsistent with the legal distinctness requirement.

B.8 Arbitration Tribunal Shall Apply the Rules in Effect at the Beginning of the Proceedings

The arbitration rules of permanent arbitration institutions are subject to changes. Therefore a question may be raised whether the rules in effect at the time when the arbitration agreement was made or the rules in effect at the beginning of the arbitration proceedings shall apply.

In the case cited above, Kalinka-Stockmann against OOO Smolensky Passazh[30] the arbitral tribunal conducted arbitration under the ICAC Rules 2005, despite the fact that the arbitration clause was included

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[29] The Constitutional Court's Resolution No. 2-P, dated 5 February 2007, relevant to the case of verifying the constitutionality of the provisions of Articles 16, 20, 112, 336, 376, 377, 380, 381, 382, 383, 387, 388 and 389 of the Code of Civil Procedure of the Russian Federation in connection with the relevant request filed by the Cabinet of Ministers of the Republic of Tatarstan, as well as complaints launched by the open joint companies Nizhnekamskneftekhim and Khasenergo and complaints from a number of private citizens.

[30] Ruling of the Federal Arbitrazh Court for Moscow Region No. KG-A40/9294-08-1,2, dated 13 October 2008.

in the agreement from 1997, before publication of the 2005 rules. The Arbitrazh Court of the city of Moscow considered this to be a breach of the arbitration procedure agreed upon by the parties, which was one of the grounds on which the ICAC award was set aside.

However the opinion of the court of the first instance that the arbitral tribunal should have applied the Rules in the version in effect at the time when the arbitration agreement was made rather than at the time when the arbitration proceedings began was not followed on appeal to the Federal Arbitrazh Court of Moscow Region.

C. INDEPENDENCE AND IMPARTIALITY OF ARBITRATORS

What follows is a review for illustrative purposes of a number of cases where the courts have considered challenges made to the arbitrations.

C.1 The Rules of an Arbitration Institution Shall Not Violate the Concept of the Equality of the Parties in Electing the Tribunal

On April 23, 2002 an Arbitral Tribunal acting under the Rules of the Arbitration Court at ZAO TPK made an award in favor of ZAO TPK. On May 23, 2002, the Arbitrazh Court of the city of Moscow issued an enforcement order, but the Federal Arbitrazh Court of the Moscow Region by its decision dated August 21, 2002[31] set aside the judgment of the Arbitrazh Court of the city of Moscow with the following reasoning.

Under the Interim Provision on the Arbitration Courts for Resolution of Economic Disputes (the "Interim Provision"),[32] in the absence of different agreement between the parties, the arbitration tribunal

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[31] Ruling by the Federal Arbitrazh Court for Moscow Region No. KA-A40/5516-02, dated 21 August 2002.

[32] Approved by the Resolution of the Supreme Soviet of the Russian Federation No. 3115-1, dated 24 June 1992. The Interim Provision was revoked under the Federal Law No. 102-FZ On Arbitration Tribunals in the Russian Federation dated 24 July 2002.

shall consist of three arbitrators. Each of the parties shall appoint one arbitrator and two appointed arbitrators shall elect the chairman. If within 15 days from the time of the notification received by one of the parties, the other party does not appoint an arbitrator, or if within the same period the appointed arbitrators do not come to an agreement on the chairman, or if the tribunal could not be established due to other reasons, the parties shall be entitled to withdraw their arbitration agreement. In that case the dispute may be referred to the state court.[33]

The applicable Rules of the Arbitration Court at ZAO TPK provided that all members of the arbitrators' panel shall be appointed by the chairman of this Arbitration Court.

The chairman of the Arbitration Court under ZAO TPK had an employment relationship with ZAO TPK, under which he received a compensation for functions performed as an employee, and on that basis the award was set aside, the court commenting: "therefore there are doubts about the impartiality of such chairman."

C.2 A Civil Servant May Not be Appointed as an Arbitrator

The arbitrazh court refused to issue a writ of execution to enforce an arbitral award issued by the panel, where one of arbitrators was a state servant.

Concerning this issue the Supreme Arbitrazh Court pointed out the following[34]:

> ...[T]he person who held a position as the court civil servant acted as an arbitrator... While this dispute was examined by the arbitral tribunal the Federal Law No. 119-FZ On the Main Principles of Civil Service in the Russian Federation re-

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[33] Article 5 of the Interim Provision.

[34] Article 25 of the Information Letter by the Presidium of the Supreme Arbitrazh Court of the Russian Federation No. 96 dated 22 December 2005 "Review of precedents characterizing the approach by the courts of arbitrazh to the cases that involve recognition and enforcement of foreign courts' decisions, contesting the decisions adopted by arbitration tribunals or issuing enforcement orders with an objective of enforcement of the judgments adopted by arbitration tribunals."

mained in effect. In accordance with Article 11 thereof a civil servant had no right to perform any other activity he would be compensated for except for teaching, scientific or other creative work. Under Paragraph 1 of the Exhibit to the Rules of the Arbitration Court the arbitrator receives compensation, *i.e.*, the performance of functions of the arbitrator is compensated. Since the activity as an arbitrator may not be qualified as teaching, scientific or other creative work such activity is not included in the list of compensated activities permitted under the Law.

C.3 Founder for One the Parties to the Dispute May not be Appointed as an Arbitrator

When a dispute under a lease agreement was examined by the arbitral tribunal the lessor had appointed as an arbitrator one of its founders (shareholders). Despite the objections by the tenant such arbitrator was not withdrawn.

The court held that the founder of the company is a person interested in the outcome of the proceedings and set aside the award.[35]

C.4 Resolution of a Dispute by an Arbitral Court with the Participation of the Party that Established such Arbitration Court Violates the Principle of "Subjective Fairness"

On 15 February 2008, Kostroma Commercial Arbitration Court established by the limited liability company Legal Services Bureau Vashe Pravo made an award in favor of this law firm and against a client of the firm.

The head of Legal Services Bureau Vashe Pravo and the chairman of the Arbitration Court was one and the same person. The case

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[35] Article 24 of the Information Letter by the Presidium of Supreme Arbitrazh Court of the Russian Federation No. 96 dated 22 December 2005 "Review of precedents characterizing the approach by the courts of arbitrazh to the cases that involve recognition and enforcement of foreign courts decisions, contesting the decisions adopted by arbitration tribunals or issuing enforcement orders with an objective of enforcement of the judgments adopted by arbitration tribunals."

was examined by a sole arbitrator appointed by the chairman of the Arbitration Court (who also signed the statement of claim).

On 11 April, 2008, the Arbitrazh Court of Kostroma Region set aside the award.

The Supreme Arbitrazh Court of the Russian Federation refused to accept the case for reconsideration, citing Article 6.1 of the European Convention of Human Rights[36]:

> At the same time the principle of court fairness represented in the principle that no one may serve as a judge for its own matter is brought forward among requirements of Paragraph 1 Article 6 of the European Convention for the Protection of Human Rights and Fundamental Freedoms by decision precedents of the European Court of Human Rights, which confirmed in its Judgment dated May 24, 1989 under the Hauschildt v. Denmark case its views that there are "two tests to determine whether a tribunal is impartial. The first is a subjective test which is based on the personal conviction of a particular judge in a given case. Second, is an objective test which ascertains whether the judge offered guarantees sufficient to rule out any legitimate doubt as to his impartiality." The implementation of the "subjective impartiality" test also implies that a person cannot be at the same time both a plaintiff and a judge in the same matter (Judgment dated November 13, 2007, Driza v. Albania) nor act under subordinate or employment relations with one of the parties (Judgment dated 22 October 1984, Sramek v. Austria).
>
> The facts established by the court and evidencing the presence of unsuitable relations between the arbitrator and a representative of the bureau, a subordination of the arbitrator to the person acting as a claimant in the dispute such arbitrator examines and the resolution of the claim by the Bureau through a tribunal it had established indicate that the arbitra-

[36] Ruling of Supreme Arbitrazh Court of the Russian Federation No. 10509/08, dated 10 November 2008.

tion tribunal was in violation of the principle of "subjective impartiality."

C.5 Examination of the Dispute by the Chairman of the Arbitration Court Appointed Without the Parties Consent Is a Violation of Principles of Independence and Impartiality

On 16 May 2007 the permanent Arbitration Court under Non-Commercial Partnership Zaschita represented by a single arbitrator, the Chairman of the Arbitration Court N., issued an award to recover from OAO Inter-Sever in favor of ZAO Center-Development indebtedness in agent fees and arbitration fees and expenses.

On 7 August 2007 the Arbitrazh Court of the city of Moscow refused to issue a writ of execution for the enforcement of the arbitral award.

The court commented that in this case the principles of independence and impartiality for arbitrators and equal standing of the parties were violated. This manifested itself in the fact that the dispute was resolved solely by the chairman of the Arbitration Court appointed without the consent of the parties, where this person was appointed by the financial director of NP Zaschita who was at the same time a shareholder of ZAO Center-Development, *i.e.* the claimant in the case.

The cassation court has upheld the decision of the court of the first instance.[37]

C.6 Non-Disclosure by Arbitrators That They Have Participated in Seminars and Conferences Organized and Paid for by a Representative of One of the Parties Casts Doubts on Impartiality and Independence

On 19 September 2006, tribunals acting under the ICAC Rules issued two awards and upheld claims of Yukos Capital against OAO Yuganskneftegaz (subsidiary of Rosneft).

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[37] Ruling of the Federal Arbitrazh Court of the Moscow Region No. KG-A40/10444-07, dated 15 October 2007.

On 23 May 2007, the Arbitrazh Court of the city of Moscow set aside both decisions. Among the grounds for the cancellation of the decisions was the following:

> Under Article 12.1 of the Law on International Commercial Arbitration, when a person is approached in connection with his possible appointment as an arbitrator, he shall disclose any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, from the time of his appointment and throughout the arbitral proceedings, shall without delay disclose any such circumstances to the parties, unless they have already been informed of them by him.
>
> As appears from the preamble of ICAC Awards Nos. 143/2005 and 145/2005, Ms. T, the managing partner of law firm N, was representing Yukos Capital S.a.r.l. Meanwhile, the law firm N, together with the Russian Chamber of Commerce and Industry, had organized an international conference on the subject "United Nations Convention on Contracts for the International Sale of Goods: 25 Years of Enforcement," and the documents of this conference were reviewed at the ICAC hearings concerned.
>
> The conference itself took place on November 7–8, 2005, and speakers there included, among others, the same arbitrators who would later sit on the arbitration panel in the above ICAC cases.
>
> The same law firm, N, took part in organizing a workshop in November 2004, in Vienna, Austria, "Hot issues in 'East-West' Arbitration," with the list of speakers again featuring the names of the arbitrators that would later consider ICAC Cases Nos. 143/2005 and 145/2005. Thus, the arbitrators had taken part in a commercial conference and a workshop sponsored, among others, by the law firm N, whose managing partner, Ms. T, subsequently represented a party to the arbitration cases under review.
>
> Failure to advise the respondent in those arbitration cases has accordingly deprived the latter of its procedural right under

> the Law on International Commercial Arbitration to challenge the arbitrator concerned.
>
> With Ms. T being the managing partner of the law firm N, her representation of the claimant in Cases Nos. 143/2005 and 145/2005 was incompatible with the fundamental principles of Russian law, such as the equality of the parties and the adversarial nature of proceedings.
>
> A breach of any such principle goes against the public policy of the Russian Federation.

Federal Arbitrazh Court of Moscow Region upheld the decision of the first instance court, commenting that such violation is not a violation of public policy but rather a violation of the arbitration procedure agreed by the parties, which shall also serve as grounds to set aside the arbitral award.

The Supreme Arbitrazh Court of the Russian Federation refused to remit this case to the Presidium and mentioned[38]:

> [T]he arbitrators who participated in examination of the disputes failed to disclose to one of the parties of the arbitration that they participated in non-commercial seminars and international conferences organized and paid for by the representative of the opposed party.
>
> They became aware of this fact only after the arbitral awards have been made. Accordingly, the representatives of OAO Yuganskneftegaz, where the company became a successor of such OAO Yuganskneftegaz, received evidence and facts that confirm the presence of unsuitable ties between the arbitrators and representatives of the company, which caused doubts about the impartiality and independence of the arbitrators.

[38] Ruling of Supreme Arbitrazh Court of the Russian Federation No. 14955/07 and No. 14956/07 dated 10 December 2007.

C.7 Participation of the Person Included in the Lists of Arbitrators of a Permanent Arbitration Institution as a Representative of the Party is not an Indicator of a Violation of the Principle of Independence and Impartiality of the Arbitral Tribunal

In the aforementioned case *Kalinka-Stockmann v. OOO Smolensky Passazh*, the Arbitrazh Court of the city of Moscow mentioned as one of the reasons for setting aside the ICAC award, "a violation of such major principle of Russian law as the principle of independency and impartiality of the court... [by] participation of Y.A. ([included] into the list of arbitrators approved by the ICAC) as a representative of one of the parties when the dispute was examined by the ICAC at the Chamber of Commerce and Industry of the Russian Federation."

The Federal Arbitrazh Court of Moscow Region did not agree with this conclusion of the court of the first instance, having mentioned that the participation of Y as a representative of the party was not in violation of the principle of independent nature and impartiality:[39]

> It is also a correct conclusion by the court of the first instance that during the examination of the case by the ICAC at the Chamber of Commerce and Industry of the Russian Federation such major legal principle as the principle of the independent nature and impartiality of the court was violated.
>
> However, the aforementioned principle was violated not through the participation of Y. included in the list of arbitrators of ICAC at the Chamber of Commerce and Industry of the Russian Federation as a representative of ZAO Kalinka-Stockmann... but rather through violating the established procedure for considering of the challenge against the chairman of the court H.D. and the arbitrator H.K. submitted by OOO Smolensky Passazh.

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[39] Ruling of the Federal Arbitrazh Court for Moscow Region No. КГ-А40/9294-08-1,2, dated 13 October 2008.

In accordance with Paragraph 3 of Article 13 of the Law of the Russian Federation No. 5338-1 On International Commercial Arbitration[40] dated July 7, 1993, further continuation of the arbitration hearing and rendering the award prior to the issue of the challenge was resolved could have taken place if the issue on the challenge had been already decided upon by the arbitration court and the party who submitted the challenge would have asked the body specified in Paragraph 1 Article 6 of the same law to make a decision with respect to such challenge.

During its session on March 31, 2008 where the respondent upheld the challenge made earlier, the ICAC Tribunal... declared that the oral hearing under the case No. 22/2007 had ended and then moved to deliberating the award, while the Presidium of the ICAC examined the challenge against the chairman of the tribunal H.D. and the arbitrator H.K. only on April 25, 2008.[41]

The party in the dispute has been granted the right of challenge in order the ensure the principle of the independent nature and impartiality of the court and therefore a violation of such principle by the ICAC when the case No. 22/2007 was examined shall also serve as the grounds to set aside the award under this case dated April 29, 2008.

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[40] Paragraph 3 Article 13 of the Law on International Commercial Arbitration: "If the challenge during the application of any procedure agreed upon by the parties or a procedure contemplated under Paragraph 2 of this Article was not upheld, the party that submitted the challenge shall be entitled, within 30 days upon receipt of the notice that the challenge was not accepted, to appeal to the body specified in Paragraph 1 Article 6 [the arbitrazh court at the location of the arbitration hearing], to make a decision concerning the challenge; such subsequent decision may not be appealed against. During the period of time while the appeal of such party is pending, the arbitration tribunal, including the arbitrator against whom such challenge was submitted, may proceed with the arbitration hearings and adopt an arbitration award."

[41] By the way, the Rules of the ICCA do not mention that the arbitration proceedings are to be suspended until the challenge against the arbitrators is considered.

C.8 Repeated Appointment by the Party of the Same Person as an Arbitrator Represents Grounds to Doubt the Impartiality of Such Person

In the aforementioned second case with participation of Kalinka-Stockmann, *Kalinka-Stockmann v. ZAO AKB Mosstroyeconombank*,[42] the Federal Arbitrazh Court of Moscow Region came to a conclusion that repeated appointment by the party of the same arbitrator casts reasonable doubts about such arbitrator's impartiality, which shall serve as the ground to set aside the award:

> We recognize as justified the conclusion of the arbitrazh court that the ICAC had violated a major principle of Russian as well as International law, the principle of independent nature and impartiality of the court.
>
> [T]his principle has been violated...through the dismissal motivated by formalistic grounds (including due to a missed deadline for objections to be filed) of the challenge against arbitrator H, where ZAO Mosstroyeconombank referred to the circumstances that can be seen as legitimate grounds to doubt his impartiality.
>
> In all cases examined by the ICAC and related to the lease of the premises in the building...ZAO Kalinka-Stockmann represented by its representative Y. selected as an arbitrator only the person H, even though it could select as an arbitrator any person having appropriate qualifications.
>
> In the opinion of the court, the persistent nature of selecting H as an arbitrator on the part of ZAO Kalinka-Stockmann serves as a legitimate basis to doubt the impartiality of such person as it demonstrates reasonable expectations by the party in the dispute that such arbitrator will support its legal position in the case.

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[42] Ruling of the Federal Arbitrazh Court of Moscow Region No. KG-A40/9254-08, dated 13 October 2008.

These circumstances allow us to come to the conclusion that during the examination of this dispute the ICAC failed to provide guarantees that the rules of the impartiality of the court would be observed.