

ARBITRATION CLAUSES IN RUSSIA-RELATED CONTRACTS: ARE YOUR DISPUTE RESOLUTION PROVISIONS FIT FOR PURPOSE?

01 August 2017 | Moscow
Legal Briefings

In December 2015, Russia passed two laws¹ which introduced a number of changes to Russia's arbitration regulation in particular, to the Arbitrazh Procedure Code, the Civil Procedure Code and the Law on International Commercial Arbitration (collectively, the "Laws"). All three entered into force on 1 September 2016.

A number of Russian court decisions over the past few years had raised doubts about the arbitrability of certain types of disputes within Russia and questions were being asked about Russia's stance towards arbitration more generally. The changes brought about by the Laws are broadly recognised as an improvement. They primarily concern disputes relating to a direct investment into a Russian company (so, an indirect investment through foreign holding structures would remain untouched by the reform), and disputes which are subject to arbitration seated in the Russian Federation. However, even within this limited scope the Laws bring clarity on a number of issues, particularly on the question of arbitrability of certain types of disputes. At the same time, they increase the powers of the Russian courts to support arbitration and whilst also providing some limits to state courts' ability to intervene.

Some of the provisions also have serious implications for the choice of a dispute resolution mechanism for parties to transactions with a link to Russia. Therefore, since the changes were introduced, many businesses involved in Russia-related contracts have been considering whether they should make changes to standard policies or practices with regard to dispute resolution choices for future contracts.

"The revised framework for Russian arbitration is largely to be welcomed. However, clients will need to navigate the complexities of certain of the new provisions in the drafting of their arbitration agreements" [Alexei Panich](#)

WHAT ARE "CORPORATE DISPUTES" FOR THE PURPOSES OF THE LAWS?

Non-arbitrable corporate disputes, arbitrable corporate disputes and implications for choice of seat and institution

Corporate disputes are generally defined as those relating to the creation and management of, and participation in, a Russian company. The breadth of this definition led to some uncertainty as to the scope of the term "corporate dispute".

NON-ARBITRABLE CORPORATE DISPUTES

The Laws have, to a degree, clarified the position and established a general presumption that corporate disputes are arbitrable. Simultaneously, the Laws provided a specific list of corporate disputes which are not covered by that presumption (ie are non-arbitrable). This list includes inter alia the following disputes:

- those relating to the convening of general shareholders meetings;
- those concerning tender offers;
- those arising out of acquisition and buy-back by a company of its own shares; and
- those connected with the expulsion of a legal entity's participants.

Specific attention was paid in the Laws to disputes relating to companies holding strategic status under the Federal Law No. 57-FZ "On Procedure for Making Foreign Investments into Entities having Strategic Importance for the State Defence and Security" dated 29 April 2008 (Strategic Law). Such disputes are generally non-arbitrable, unless related to ownership over shares or interests, the transaction of which did not require approval under Strategic Law.

Non-arbitrable corporate disputes shall be determined by the Russian arbitrazh (state) courts at the place of the Russian target company's business.

ARBITRABLE CORPORATE DISPUTES

Group 1:

Examples include disputes arising out of: the incorporation, reorganisation and liquidation of legal entities; claims by shareholders to recover damages caused to a legal entity and for the invalidation of transactions made by a legal entity; and agreements relating to the management of a legal entity, such as Shareholders Agreements.

Group 1 corporate disputes must:

- be administered by a "permanent arbitration institution" (see further below);
- have a seat in Russia;
- be heard in accordance with special rules of procedure for corporate disputes to be adopted by such institutions; and
- be subject to an arbitration agreement between the legal entity itself, all shareholders / participants and other parties who are to be claimants / defendants.

Group 2:

This category includes disputes regarding ownership over shares, interests in legal entities, the creation of encumbrances over such shares/interests or the exercise of rights arising therefrom (eg SPAs).

Group 2 corporate disputes must be administered by a permanent arbitration institution, but need not have a seat in Russia.

KEY CHANGES

1. Positive changes to the laws

Increased court powers:

- to appoint arbitrators and deal with challenges to arbitrators
- to assist in the taking of evidence

Arbitration agreements:

- clearer requirements as to electronic form arbitration agreements
- pro-arbitration bias: any doubts to be interpreted in favour of validity and enforceability
- arbitration agreements may be included in the charter of a legal entity provided that this is approved by all of the entity's shareholders. An arbitration agreement may not be included in the charter of a public joint company or a joint stock company with 1,000 voting shareholders or more.
- an arbitration agreement continues to be in effect in the event of assignment of the principal contract to a new creditor / debtor.

2. Arbitrability of disputes in Russia

As a rule, all disputes now are arbitrable, unless otherwise envisaged by law. The Laws set out a (non-exhaustive) list of disputes that are non-arbitrable, including:

- bankruptcy cases;
- administrative disputes;
- labour disputes;
- class actions;
- disputes relating to public procurement (until such time as a specific law governing arbitral procedure in relation to such type of disputes is introduced); and
- corporate disputes.

ENTERING INTO AN ARBITRATION AGREEMENT FOR AN ARBITRABLE CORPORATE DISPUTE

Arbitration agreements with scope to cover arbitrable corporate disputes may be validly concluded only after 1 February 2017. Those concluded before 1 February 2017 but after 1 September 2016 (the date when the Laws entered into force) are treated under the Laws as inoperable, with the result that the Russian arbitrazh (state) court may take jurisdiction over the substance of any dispute.

Further, the position is not straightforward with regards to arbitration agreements concluded before 1 September 2016. It is not sufficiently clear now whether the above restriction has retrospective effect, and applies to arbitration agreements entered into before the Laws came into force (ie before 1 September 2016). However, in any event, reliance on any existing arbitration agreement which is inconsistent with the new Laws adds significant risks, particularly with regard to the enforceability of any award rendered under such agreement.

On this basis, it is advisable that all arbitration agreements in Russia-related contracts concluded before 1 September 2016 are reviewed and amended to ensure that all corporate disputes are referred to a permanent arbitration institution, and are seated in the Russian Federation where mandated by the Laws.

WHAT IS A "PERMANENT ARBITRATION INSTITUTION" UNDER THE LAWS?

As described above, arbitration of Russian corporate disputes (whether or not seated in Russia) and arbitration of all Russia-seated disputes (regardless of what the dispute relates to) may only be administered by a permanent arbitral institution (a PAI). To be a PAI, an arbitration institution requires a permit (or licence) from the Government of the Russian Federation. Whilst the approach may appear, on its face, protectionist, it has been introduced to try to avoid the conflicts of interest that have arisen when corporations set up their own "pocket" institutions to administer disputes to which they are party.

However, a consequence of this approach is that parties may not be able to choose their favoured international arbitral institution for resolution of Russian corporate or Russia-seated disputes. Many of the international arbitral institutions have not yet decided whether to apply to the Russian Government for a licence as a PAI. At a recent arbitration conference held by the Russian Arbitration Association in Moscow, it was confirmed that the Vienna International Arbitration Centre (VIAC) and the Kuala Lumpur Regional Arbitration Centre (KLRCA) have decided to register. At the same event, representatives from the ICC, SCC, HKIAC, SIAC and Swiss Chambers' Arbitration Institution indicated that those institutions were undecided or considering their approach. Anecdotal feedback suggests that the institutions are hesitant to risk being seen to compromise their independence by virtue of registration and are also considering the tax implications.

It should be noted that the International Commercial Arbitration Court at the Russian Chamber of Commerce and Industry (ICAC) is exempt from the licensing requirement and may administer Russian corporate disputes.

PLANNING AHEAD ARBITRATION CLAUSES WHICH CONTEMPLATE REGISTRATION OF INSTITUTIONS IN THE FUTURE

Many commercial parties are accommodating the uncertainty as to which institutions will be a PAI into their arbitration agreements. For instance, the parties often agree on an arbitration clause which provides for dispute resolution by the ICAC (or another licensed institution at the signing date) by default, with another preferred institution to take the place of the ICAC for any disputes which arise after that institution becomes eligible to hear corporate disputes. To maximise the chances of an arbitration being administered by a preferred institution, the parties can provide for a certain priority ranking (eg LCIA – first priority, ICC – second priority, etc.) in the arbitration agreement.

OTHER IMPORTANT DRAFTING POINTS FOR RUSSIAN-RELATED ARBITRATION AGREEMENTS

When drafting arbitration agreements which provide for a Russian seat, it is important to be aware that certain provisions may not be incorporated by reference (including certain of the chosen institutional arbitration rules). Rather, such provisions require express and direct agreement by the parties. For example such direct agreement may prohibit any assistance by the Russian courts in appointment of the tribunal in cases where the appointment mechanism fails.

Parties may also expressly exclude by direct agreement the right to apply to a Russian court to challenge the tribunal's jurisdiction and the right to apply to set aside an award, including on the grounds of public policy. Many commercial parties are keen to exclude any potential for court challenges to the extent possible and it is important to note that this must be done expressly.

Make sure that reference is made to a particular arbitral institution, not only to the rules of that institution. This point arose from a decision of the Russian court.² Although this position was further overruled by the higher court,³ it is still recommended to mention the arbitration institution itself in arbitration clauses in order to avoid any risk of the arbitration agreement being found to be unenforceable.

A MIXTURE OF CORPORATE AND NON-CORPORATE DISPUTES: DEALING WITH CONSOLIDATION OF MULTIPLE ARBITRATIONS

The particular requirements as to corporate disputes lead to further drafting complexities when the transaction in question could lead to both corporate and non-corporate disputes and the parties wish to include the possibility to consolidate the arbitrations arising under different related agreements. Despite the modernisation of the legal framework in Russia, many parties remain reluctant to select Moscow as a seat of arbitration unless they are obliged to do so by Russian law. However, in certain circumstances consolidation provisions could fail, for example, when parties have agreed on a foreign seat but are required by the Laws to arbitrate part of their dispute in Russia. It may also lead to potential problems with conflicting decisions from different tribunals.

It will be important to consider the best solution in the circumstances of any particular transaction, considering whether corporate and non-corporate disputes will arise under the same factual matrix. This will depend on a number of factors, including the likelihood of inter-related corporate and non-corporate disputes arising, and the priority which the parties give to the seat of arbitration.

Many parties have historically been wary of selecting Moscow as a seat of arbitration, because (inter alia) of the risk of interference in the process from the Russian courts. Despite the uncertainties and complexities as described above, the reforms constitute a well-intentioned, significant and positive step towards increasing confidence in the choice of arbitration in Russia. A consistent interpretation of the Laws by the Russian courts over the next few years, demonstrating judicial support for arbitration would further assist Moscow in attracting international parties to arbitrate there.

To discuss whether your dispute-resolution provisions in Russia-related agreements require amendment, please contact Alexei Panich or Nick Peacock, or your usual Herbert Smith Freehills contact.

FOOTNOTES

1. The Federal Law On Arbitration (Arbitration Proceedings) in the Russian Federation and the Federal Law on Amendments to Certain Legislative Acts.
2. Resolution of Moscow circuit Federal Arbitrazh Court dated 13 March 2012 in the case No. A40-29251/11-68-256, A40-21119/11-68-183.
3. Resolution of the Presidium of Russian Supreme Arbitrazh Court dated 16 July 2013 No. 2572/13.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



ALEXEI PANICH
PARTNER /
ADVOCATE /
CHAIRMAN OF
HERBERT SMITH
FREEHILLS COLLEGE
OF ADVOCATES,
MOSCOW
+7 495 363 65 15
alexei.panich@hsf.com



**ALEXANDER
GRIDASOV**
SENIOR ASSOCIATE,
MOSCOW
+7 495 36 36536
Alexander.Gridasov@hsf.com



HANNAH AMBROSE
SENIOR ASSOCIATE,
LONDON
+44 20 7466 7585
Hannah.Ambrose@hsf.com



VANESSA NAISH
PROFESSIONAL
SUPPORT
CONSULTANT,
LONDON
+44 20 7466 2112
Vanessa.Naish@hsf.com

LEGAL NOTICE

The contents of this publication are for reference purposes only and may not be current as at the date of accessing this publication. They do not constitute legal advice and should not be relied upon as such. Specific legal advice about your specific circumstances should always be sought separately before taking any action based on this publication.

© Herbert Smith Freehills 2021

SUBSCRIBE TO STAY UP-TO-DATE WITH INSIGHTS, LEGAL UPDATES, EVENTS, AND MORE

Close

© HERBERT SMITH FREEHILLS LLP 2021