

Kluwer Arbitration Blog

The US\$50 billion Yukos award overturned - Enforcement becomes a game of Russian roulette

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Introduction

The Hague District Court ruled on 20 April 2016 to reverse a PCA tribunal's decision against Russia to pay damages in excess of US\$50 billion to the former majority shareholders of Yukos Oil Company, which was once the largest oil company in Russia (see earlier [blog post](#) on the Hague Court's decision). The Hague Court held that there was no valid arbitration agreement and therefore, the PCA tribunal did not have jurisdiction in the arbitration brought against Russia under the Energy Charter Treaty (ECT). The annulment decision will inevitably have an impact on enforcement proceedings already underway in different jurisdictions against Russia's assets.

In a big ticket arbitration where costs reach unprecedented highs (in the *Yukos* arbitration, the tribunal ordered Russia to pay US\$60 million in legal fees to Yukos's lawyers), waiting an inordinately long time for justice to take its course has not gone unnoticed. Commentators have criticised the inefficiency and the extremely slow progress of the *Yukos* case. To have the jurisdiction of the PCA tribunal rejected ten years after proceedings were commenced does not amount to justice. Irrespective of the outcome, justice delayed is justice denied. In this note, the authors examine the possible consequences of the Hague Court's decision.

Background

The dispute between Yukos and Russia started with Moscow's pursuit of Yukos and its chief executive, Mikhail Khodorkovsky for alleged tax evasion. Following the dissolution of Yukos by Russian authorities in 2003 and the arrest of Mikhail Khodorkovsky, Yukos's majority shareholders - Hulley Enterprises, Yukos Universal and Veteran Petroleum - commenced arbitration against Russia. The claimants alleged that Russia had breached its obligations under the ECT through a series of actions which eventually saw the transfer of Yukos's assets to state-owned energy giants, Rosneft and Gazprom.

In July 2014, a PCA tribunal consisting of Yves Fortier QC, Charles Poncet and Stephen Schwebel ordered Russia to pay damages in excess of US\$50billion to the

former Yukos majority shareholders. The tribunal held that Russia had launched “*a full assault on Yukos and its beneficial owners in order to bankrupt Yukos and appropriate its assets while, at the same time, removing Mr. Khodorkovsky from the political arena*”. The award was 20 times bigger than any previous arbitral award and equivalent to 20 per cent of Russia’s annual budget.

The Hague Court’s Ruling

Russia challenged the award before the Hague District Court being the court of the seat of arbitration. The Hague Court quashed all six arbitration awards (three interim awards and three final awards) against Russia. This was the first time in 20 years that the Hague Court had overturned an arbitral award.

The Hague Court found that the PCA tribunal had no jurisdiction over a claim brought under the ECT, which Russia signed in 1994, but never ratified. The Hague Court concluded that Moscow had not agreed to be bound by the ECT’s provisional application and certainly not Article 26, which gives the necessary ground for submitting disputes to arbitration.

Enforcement challenges

After the PCA tribunal’s award, the former Yukos majority shareholders started enforcement proceedings against Russia’s overseas assets in a number of countries including France, Belgium, Germany, the UK, the US and India.

However, such enforcement efforts had already run into problems. A Paris court invalidated the seizure of 400 million euros that French company Eutelsat owed to Russian company RSCC for satellite cooperation deals. The same court also annulled the seizures against Russian news agency, Sputnik and the Russian agency for management of state property abroad. Another Paris court had invalidated seizures at France’s Arianespace, which owed hundreds of millions of euros to Russian state space agency Roscosmos. The court held that Roscosmos was a separate legal entity from the Russian state and therefore could not be held liable for Russia’s debts.

Proceedings are underway in nine other French courts and the Paris court decisions are being appealed against with the result that the Russian assets remain frozen. In total, some US\$1 billion worth of Russian assets were frozen in France and Belgium alone. However, Belgium had unfrozen the bank accounts of several Russian state entities operating in the country. And Russia managed to persuade Belgium to pass a ‘Yukos law’ requiring that a judge pre-authorises attachment of assets and thereby enhancing its sovereign immunity protection. It has been reported that France may follow suit with a similar piece of legislation.

The Hague Court ruling would surely now make enforcement against Russia’s overseas assets even more challenging. Welcoming the ruling, Vladimir Putin’s spokesman Dmitry Peskov said, “*We expect that the enforcement of the (original) ruling will be stopped immediately in all countries.*” It remains to be seen whether existing enforcement proceedings will actually be stopped in various jurisdictions.

Article V(1)(e) of the New York Convention states that a country may refuse to enforce

an award if it has been set aside by a court at the seat of arbitration. The wording of the relevant provision is below:

“Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority proof that....

(e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.” (Emphasis added).

The New York Convention’s use of the word “*may*” provides for a discretionary standard rather than a binding one. It is therefore upon national courts’ discretion to either observe the Hague Court’s ruling and refuse enforcement or recognise and enforce the arbitral award.

The French position is that a setting aside by a court at the seat of arbitration should be disregarded altogether on the basis of its own domestic laws. As for enforcement in the US, it has been suggested that the setting aside of the arbitral award in the Hague Court is a defence under Article V(1)(e) as enshrined in the US Federal Arbitration Act. In an article on the New York Convention, Albert Jan van den Berg, who was incidentally counsel for Russia in the Hague Court, stated that “...*the vast majority of the courts in the other Contracting States do not enforce arbitral awards that have been set aside in the country of origin, either under the Convention or otherwise*”. However, there is a significant amount of recent case law where courts have recognised foreign awards annulled at the seat of arbitration.

Interestingly, in a previous case, *Yukos Capital v OJSC Rosneft Oil Co* involving a different Yukos entity, both English and Dutch courts recognised an arbitral award in circumstances where Russian courts (courts at the seat of arbitration) had annulled the arbitral award that Yukos Capital was seeking to enforce. It was held that Russian courts’ annulment of the arbitral award was the result of a “*partial and dependent judicial system*”. Such an allegation is unlikely to be levelled at the Hague Court.

Despite the setback from the Hague Court ruling, lawyers for the former Yukos shareholders stated that they will continue to proceed with enforcing the arbitral award against Russia with the hope that enforcement courts will have liberty to assess the arbitral award for themselves. They also confirmed that they would be exercising their right of appeal to the Court of Appeal in the Hague. Furthermore, there could also be an appeal to the Supreme Court of the Netherlands. This entire process could take up to five years to complete.

Conclusion

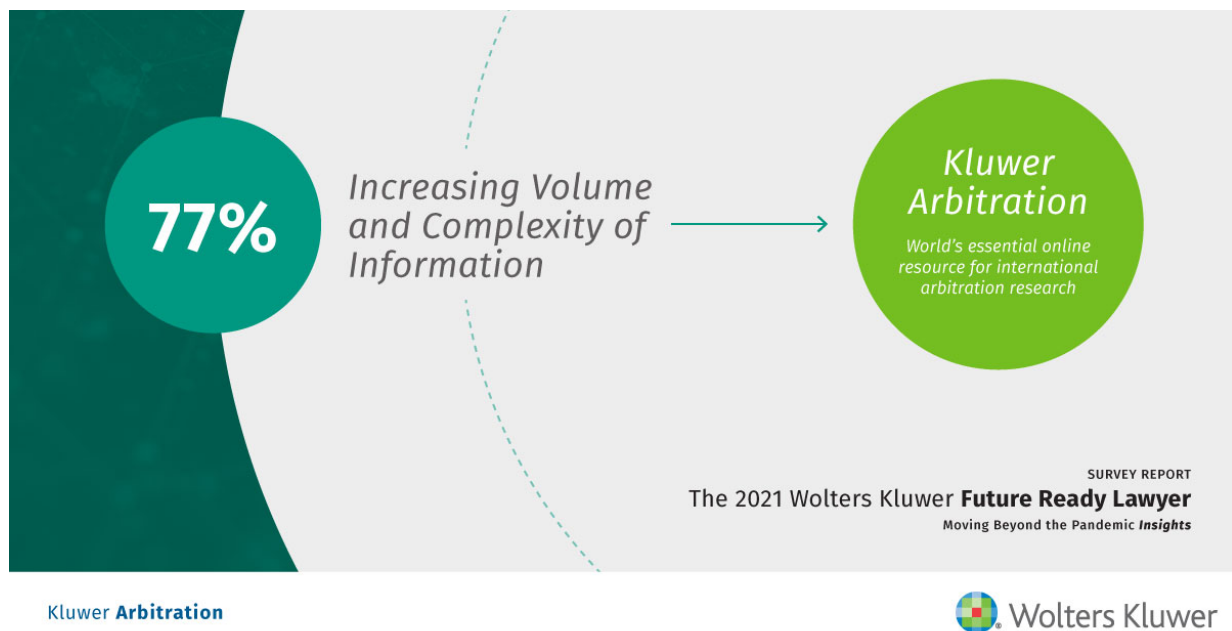
The Yukos case started more than a decade ago and has further to go in terms of the Hague Court proceedings and enforcement proceedings in multiple jurisdictions. What lies ahead is hard to predict especially given wider political issues involving Russia. However, Yukos is turning into a case for the arbitral community to test its limits and set new precedents.

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