New Exclusive Competence of Russian Courts in International Sanctions-Related Disputes: Is It as Bad as It Sounds?

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As a result of coronavirus, sanctions, for once, have not been grabbing the headlines. Unlike the media, the Russian legislative bodies have recently shown keen interest in the topic of sanctions as they have adopted a draft law from last year granting persons and companies affected by the sanctions against Russia with a right to transfer all international disputes to Russia. The law also penalizes counterparties if they seek to oppose to such a transfer. For the international arbitration community, the adoption of this law could be a cause for concern because, despite a valid arbitration agreement, individuals and companies affected by the sanctions against Russia may bring their disputes to Russian state courts, obstruct the already existing proceedings and resist the enforcement of foreign awards on the basis of the new law.

What is the New Law All About?

The new law grants Russian state courts with exclusive competence regarding all

disputes involving Russian persons or companies, as well as foreign companies affected by sanctions against Russia, unless otherwise agreed in the arbitration agreement or international treaty. The same goes for disputes which emerged due to such sanctions: Russian courts will have exclusive competence regardless of the nationality of the individual or the company.

One might breathe a sigh of relief after spotting the words "*unless otherwise agreed*…", but the law continues that it is also applicable if a dispute resolution agreement in favor of international commercial arbitration (or a foreign court) has become incapable of being performed due to sanctions. It follows from the law, however, that it does not affect jurisdiction established by foreign treaties.

Thus, the law grants two mechanisms to the sanctioned parties.

First, if the sanctioned party is a claimant and no foreign proceedings are pending, it may submit its claim with a Russian state court.

Second, if there are some foreign proceedings pending or if it is evident that they will be initiated (e.g. a foreign claimant has sent a pre-trial demand), the sanctioned party may apply to a Russian court for an anti-suit injunction. The court considers whether to grant such injunction in a court hearing.

Additionally, the Russian court may order the disobeying party to pay to the sanctioned entity a sum of money up to the total amount in dispute as well as the legal costs, if the granted injunction is ignored.

Needless to mention, a foreign award (or court decision) ignoring the sanctioned party plea to terminate the proceedings and "transfer" them to Russia will be unenforceable in Russia.

The new law does not have any specific rules regarding its application in time, which means that, being of procedural nature, new rules may be applied immediately after the entry into force (i.e. including to the arbitrations which are currently pending).

Is It Really That Scary?

In general, the new law will mostly affect only those adversaries of the sanctioned

entities which have assets in Russia and/or which plan to enforce their awards there.

Firstly, the rules contained in the new law are of procedural nature and do not have extraterritorial effect. This means that they are not mandatory in foreign jurisdictions and will not necessarily prevent the enforcement of awards (and foreign court decisions) in countries other than Russia.

Secondly, pecuniary "fine" in favour of a sanctioned entity for failure to terminate foreign proceedings in accordance with the injunction is unlikely to be enforceable anywhere except Russia. This is at least because the nature of such judicial acts is unlikely to be treated as a final court decision (let alone the probability that a foreign court would anyway consider such injunction contravening its public policy and undermining the access to justice of the sanctioned party's adversary).

If the adversary of the Russian entity does not plan to enforce an award there and does not have any assets in Russia which may be recovered for his disobedience, the new law does not pose significant risks.

The suggested anti-suit injunction mechanism itself will also be quite burdensome to materialise. The reason for this is that Russian courts take conservative approach to the service of process. Despite being signatory to the Hague Convention and having dozens of bilateral treaties, service of process on foreign parties in Russia still takes not less than 6-9 months. This is partly because the service of process on foreigners itself is unfamiliar to some Russian courts and takes them significant time to properly accomplish. Partly this is a result of general refusal of courts to apply methods of service which are fast enough (e.g. courier post, rather than regular mail). All in all, a period of 6-9 months gives a chance for some arbitrations to be completed.

Furthermore, a Russian court decision rendered in relation to the claim of a sanctioned entity in disregard of an arbitration agreement (on the basis that it became incapable of being performed due to sanctions) might also be hard to enforce abroad. The reason for this lies in the fact that Russia does not have many bilateral agreements to this end and is not a party to any global convention (such as Convention of 2 July 2019 on the Recognition and Enforcement of Foreign Judgments in Civil or Commercial Matters, which has not yet entered into force in any case). Additionally, a decision of the Russian court is likely not to be heeded in

foreign jurisdictions on the ground that a Russian court should not have considered a dispute in disregard of the parties' arbitration agreement.

The New Law – A True Novelty or Not?

It has to be noted, however, that even before the adoption of this new law the Russian courts already allowed sanctioned entities to overcome arbitration agreements and bring disputes to Russia.

For instance, in case A40-149566/2019, the appellate court upheld the decision of the Commercial Court of Moscow to grant the claim and to amend the ICC arbitration clause in the contract to state that all disputes shall instead be referred to the Russian courts. The courts found that, since the claimant was included by the Office of Foreign Assets Control (OFAC) to the SDN list,[fn]*Specially Designated Nationals and Blocked Persons List* is a list of persons whose assets are blocked and with whom U.S. persons are generally prohibited from dealing with.[/fn] the enforcement of an ICC award anywhere in the world except Russia would be impossible. Due to this, the courts held that the dispute has to be resolved in the Russian court. This logic seems to be flawed because the courts confused the enforceability of the arbitration clause with the enforceability of the arbitration award. An ICC award, corresponding to the parties' agreement, could also be potentially enforced in Russia. Moreover, a Russian court judgement is likely to encounter the same difficulties as an ICC award with enforcement abroad.

The case is currently before the Commercial Court of Moscow Circuit. However, the new law is expected to significantly favor the position of the Russian claimant.

Concluding Remarks

While sanctions are known to cause major difficulties for the parties, arbitration institutions hold the view that they are able to overcome them (e.g. by opening special accounts in order to facilitate the payment of the arbitration fees). If sanctions frustrate the access of the sanctioned entity to justice to such an extent that the agreed arbitration is no longer available (incapable of being performed), proceedings at the competent state court shall still be in available. However, the

new law allows to disregard the usual rules and to transfer any dispute to a Russian court. As a result, foreign investors have to always consider a risk of being compelled to adjudicate disputes in Russian state courts if the Russian counterparty is under the sanctions. This, of course, may negatively affect the investment climate.