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The Supreme Arbitrazh Court of the Russian Federation rules on the validity of dispute resolution clauses with a unilateral option

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Introduction

On 19 June 2012 the Presidium of the Supreme Arbitrazh Court of the Russian Federation ("**SAC RF**") issued a decree ("**Decree**") in case No. VAS-1831/12 in which it examined the validity of an optional jurisdictional clause. The full text of the Decree setting out the rationale for the decision was published on 1 September 2012.

The Presidium of the SAC RF found that a dispute resolution clause under which all disputes between the parties to the contract are referred to international arbitration and one of the parties is granted the option to refer disputes to the competent state courts ("**Unilateral Option Clause**") violates the principle that the parties to a dispute have equal procedural rights. Although the Decree is not entirely clear as to the effect of such clauses, interpretation of the Decree suggests that the Presidium of the SAC RF ruled that where the parties have entered into a Unilateral Option Clause both of them (not just one) have the right to choose (depending on which one of them is the claimant) between international arbitration and state courts. Effectively, the Presidium of the SAC RF has converted the "unilateral option" in such clauses to a "bilateral option".

The dispute

In May 2009 the Russian company Russkaya Telefonnaya Kompaniya ("**RTK**") and Sony Ericsson Mobile Communications Rus, a Russian subsidiary of Sony Ericsson ("**Sony Ericsson**"), entered into a contract for delivery of mobile phones. The dispute resolution clause in the contract called for all disputes between the parties to be resolved through ICC arbitration in London. Sony Ericsson, however, had an option to apply to a court of competent jurisdiction with a claim for recovery of outstanding amounts for the goods delivered ("**Dispute Resolution Clause**").

RTK had complaints as to the quality of the goods and filed a claim against Sony Ericsson with the Arbitrazh Court of the City of Moscow seeking the delivery of replacement goods. Sony Ericsson, invoking the Dispute Resolution Clause, moved that RTK's claim should be left without consideration.

The lower courts' conclusions

The Arbitrazh Court of the City of Moscow granted Sony Ericsson's motion and ruled on 8 July 2011 to leave RTK's claim without consideration on the basis of Article 148(1)(5) of the Arbitrazh Procedure Code of the RF.
RTK appealed the ruling, arguing that, among other things, the Dispute Resolution Clause violated Russian Federation public policy, as it contravened the principle that the parties to a dispute have equal procedural rights. By the decree of the Ninth Appellate Arbitrazh Court dated 14 September 2011 the appeal was dismissed. The appellate court found that the Dispute Resolution Clause was not invalid, as the parties had the right to agree on such a dispute resolution procedure in accordance with the principle of freedom of contract.

In its decree dated 5 December 2011 the Federal Arbitrazh Court of the Moscow District upheld the judicial acts of the lower courts. (It should be noted that previously Russian courts also upheld the validity of dispute resolution clauses with a unilateral option. See for example, decree of the Federal Arbitrazh Court of the Northwest District dated 23 September 2004 in case No. A21-2499/03-C1).

RTK filed a supervisory appeal with the SAC RF. On 28 March 2012 a panel of three Supreme Arbitrazh Court judges issued a ruling stating, among other things, that in their view the Dispute Resolution Clause violated the principle of procedural equality of the parties, and they decided that the case should be transferred to the Presidium of SAC RF to be decided.

The Decree of the Presidium of the SAC RF

The Presidium of the SAC RF found, with reference to the decrees of the Constitutional Court of the Russian Federation, that one of the guarantees of fair dispute resolution is that the parties should have equal rights to present their positions to the courts or other adjudicatory authorities (including arbitral tribunals) and that the principles of adversarial proceedings and procedural equality of the parties mandate that the parties should have equal procedural opportunities. The Presidium of the SAC RF also cited in support of its findings the European Convention on Human Rights 1950 and decisions of the European Court of Human Rights (*inter alia Batsanina v. Russia, Sokur v. Russia and Steel and Morris v. The United Kingdom*).

The Presidium of the SAC RF thus concluded that "*based on the general principles of protection of civil law rights, an agreement on dispute resolution cannot grant only one party (the seller) under a contract the right of recourse to a competent state court and deprive the second party (the buyer) of an analogous right. Where such an agreement is concluded, it is invalid as violating the balance of the parties' rights. Accordingly, a party whose right is infringed by such an agreement on dispute resolution also has the right of recourse to a competent state court, having exercised the guaranteed right to judicial protection on equal terms as its counterparty*".

It is not entirely clear in such cases whether the entire dispute resolution clause including the arbitration agreement should be deemed invalid or just the provision that only one party can opt to resort to the state courts (in which case either party when bringing a claim could decide to refer the dispute to ICC arbitration or to the competent state courts). On interpretation of the Decree, however, we believe the latter is likely to be the case.

The Presidium of the SAC RF set aside the judicial acts of the lower courts and sent the case back for reconsideration. The Decree has retrospective effect, i.e. any previous judicial acts under which

a party was denied the right to have a claim heard by a state arbitrazh court on the basis of a Unilateral Option Clause will now be subject to reconsideration on the basis of newly discovered circumstances.

It may be worth mentioning that earlier this year the Presidium of the SAC RF confirmed the validity of dispute resolution clauses which provide that any party acting as claimant has the right to refer disputes to either a state court or a domestic arbitral tribunal (i.e. dispute resolution clauses with "bilateral option") (decree of the Presidium of the SAC RF No. VAS-11196/11 dated 14 February 2012). With the recent Decree, the Presidium of SAC RF has effectively converted the "unilateral option" in Unilateral Option Clauses into a "bilateral option".

Conclusions

On the basis of our interpretation of the Decree we do not believe it is likely that enforcement of arbitral awards based on Unilateral Option Clauses should be jeopardized by the Decree in Russia. Unless there exist special circumstances, the position of the Presidium of the SAC RF is that, notwithstanding the "unilateral option" in a Unilateral Option Clause, any party acting as claimant has the right to choose between international arbitration and litigation. Thus, if the claimant decides to refer a dispute to arbitration, the arbitral award should not be vulnerable to being challenged on the basis of inequality.

At the same time, the Decree opens the door to parallel proceedings in Russia aimed at torpedoing arbitration proceedings. Currently, parallel proceedings in Russian courts are commonly used by Russian respondents as a means of avoiding enforcement of arbitral awards in Russia. A typical example is when court proceedings are initiated by a minority shareholder of a respondent in an arbitration who is seeking invalidation of an agreement in relation to which claims have been brought in arbitration. Given that the Decree effectively converts "unilateral options" to "bilateral options", Russian respondents (who were generally not the parties to whom "unilateral options" were granted) will no longer need to initiate shareholder claims in order to commence proceedings in Russian courts. It is also uncertain whether or not Russian courts will be inclined to stay parallel proceedings after arbitration has been commenced: under Russian law they have only a discretionary right rather than an obligation to do so.

To conclude, as a result of the Decree only "pure" arbitration clauses will have the effect of precluding a counterparty from bringing disputes to Russian courts (to the extent such disputes are arbitrable).

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