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Extension of Exclusive Jurisdiction of Russian State Courts over Disputes Involving Sanctioned Persons: Protection of National Interests or a Threat to Party Autonomy?

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On 19 June 2020, the new sanctions-related amendments[1)] to the Russian Commercial (Arbitrazh) Procedure Code entered into force. The main objective of the law is to protect the interests of Russian natural and legal persons who are unable to effectively resolve their disputes in court or arbitral proceedings outside Russia due to the imposition of foreign sanctions.

According to the amendments, Russian commercial courts have exclusive jurisdiction over cases where one of the parties (Russian individual and legal entity, or foreign legal entity) is subject to foreign sanctions or where the dispute itself arises out of foreign sanctions. The exclusive jurisdiction of Russian courts can be changed by an international treaty or a dispute resolution agreement unless the latter is held unenforceable as a result of impediments in "access to justice" as a consequence of foreign sanctions.

Amendments also stipulate that Russian commercial courts can issue anti-suit injunctions preventing a party to initiate or continue foreign arbitration proceedings or court litigation. Before the introduction of the amendments, Russian courts were reluctant to issue anti-suit or anti-arbitration injunctions, even though the Russian Commercial (Arbitrazh) Procedure Code contains a non-exhaustive list of interim measures, including those that prohibit a party from taking certain actions.[2)] Courts are now expressly authorized to grant such injunctions, but only in relation to a narrow type of disputes falling within the scope of the sanctions-related amendments. To obtain an injunction, a party has to show that Russian courts have exclusive jurisdiction, the dispute resolution agreement (if any) is unenforceable, and that foreign proceedings have been commenced or are planned to be initiated. Non-compliance with the injunction may result in the decision on damages not exceeding the entire amount of the claim plus legal expenses.

The law is expected to have paramount importance for arbitration as it is formulated in a broad and ambiguous way, allowing parties to ignore valid arbitration agreements for tactical considerations and transfer disputes from the pre-agreed forum to Russian state courts.

Areas of Concern

At first sight it seems that the amendments indeed improve the position of sanctioned individuals and entities. However, a closer look reveals that they are vaguely formulated and leave a number of questions open.

First, the scope of the amendments is excessively broad. Strictly speaking, the amended provisions use the term “restrictive measures” rather than “sanctions”. While the primary goal of the amendments is to protect Russian business negatively impacted by foreign sanctions, especially the US and EU ones, the vague language allows to apply the relevant articles when “any restrictive measures” are imposed against Russian individuals and legal entities. The law does not differentiate between the types of measures and arguably applies to secondary sanctions, sectoral sanctions, individual lists etc. Further, the law expressly states that respective measures may be taken by any foreign states, association or union of states, governmental (intergovernmental) institution of a foreign state, association or union of states.

Consequently, it is extremely difficult, if not impossible, to predict at the time of negotiating the contract, whether the Russian counterparty may be potentially subject to such restrictive measures. Moreover, foreign parties may find themselves in a situation where they are forced to litigate disputes which have no genuine connection with Russia before Russian state courts.

Second, the amendments apply both to litigation and international arbitration outside Russia. It is evident that litigation outside Russia means litigation in a foreign court. However, it is not entirely clear what is meant by “arbitration outside Russia”. It may cover all foreign-seated arbitrations irrespective of whether the proceedings are administered by foreign or Russian arbitral institutions. Alternatively, the amendments may cover arbitrations administered by foreign arbitral institutions, including the ones with a seat in the territory of Russia. If the latter interpretation is adopted, local-seated arbitrations conducted under the auspices of HKIAC or VIAC (which have received the status of permanent arbitral institutions from Russian government to administer certain types of disputes) might still qualify as “arbitrations outside Russia” for the purpose of the amendments.

Third, there is a risk that the respective sanctions-related changes will apply retrospectively to the agreements concluded before the introduction of the amendments. This may result in a number of contracts with Russian counterparties being renegotiated or, in the worst-case scenario, terminated in the near future.

Last but not least, amendments give the sanctioned party an opportunity to circumvent the binding effect of the arbitration agreement by claiming that it is “incapable of being performed” for the reason that the application of restrictive measures creates obstacles in the access to justice for such a party. This is arguably the most controversial amendment. There is no clarification on what may constitute obstacles in the access to justice and what standard of proof should be applied by the courts when dealing with such an allegation. It is reasonable to assume that the court should require the sanctioned person to present evidence that the latter is facing objective hurdles in handling a dispute in a foreign forum, such as the impossibility to appoint an arbitrator who would agree to resolve a dispute involving sanctioned persons or refusal of the relevant forum to accept the dispute as such. The mere difficulties experienced by a sanctioned entity, including delays on the part of arbitral institution in accepting the payment of the deposit or the necessity to receive permits from relevant organs to process the payment, should not be considered sufficient to render the arbitration clause unenforceable.

However, there is a fear that Russian courts will interpret the provision in an extremely broad way.

In a recent case the ICC arbitration clause was held incapable of being performed, since the imposition of US sanctions on claimant amounted to a fundamental change of circumstances, justifying the transfer of the dispute to the Russian state court.[3)] The decision was upheld in both appeal and cassation instances. Thus, there is a risk that sanctioned persons may take advantage of the sanctions-related amendments to escape agreed dispute resolution clauses.

Practical Considerations

While trying to protect Russian business in the first place, the amendments are likely to make Russian companies less attractive in the eyes of their foreign partners. Given the protectionist approach of lawmakers and the interventionalist attitude of Russian courts towards arbitration, the amended provisions may be used as a tool to block enforcement of foreign arbitral awards and get more favorable judgements from Russian courts.

However, the negative impact of sanctions-related changes is limited, as the law lacks extraterritorial effect. Hence, it will only significantly affect foreign companies / individuals that have assets in Russia or the ones that will need to enforce foreign arbitral awards or judgements in the territory of Russia. Consequently, this may serve as an incentive for foreign companies to pull their assets out of Russia or decrease their amount in the country.

Moreover, the amendments may trigger parallel proceedings and subsequent fragmentation of disputes with decision-makers in foreign forum going ahead with cases despite the mandatory provisions of Russian law. The amended provisions clarify that the enforcement of foreign awards and judgements rendered in violation of the rules on exclusive jurisdiction of Russian courts is still possible, but only on condition that a sanctioned person has itself initiated enforcement proceedings or has not raised objections concerning the lack of jurisdiction of a foreign court or arbitral tribunal, including the situations where a sanctioned person has not requested anti-suit injunctions from a competent commercial court in Russia.

Further, given the fact that anti-suit injunctions requests shall be considered in a court hearing with notification of all relevant parties (which might take quite a long time), the chances that the foreign award or judgement will be issued before the injunction is granted slightly increase. In this scenario, the award will be enforceable abroad, but the party might still experience difficulties with enforcing the award in Russia. The same applies to annulment proceedings: breach of the injunction or its consideration by the Russian court is more likely to impact the annulment of the award if the seat is in the territory of Russia.

Finally, the application of the sanctions-related amendments can be excluded by providing for arbitration clauses in favor of domestic arbitration, better both seated in the territory of Russia and administered by local arbitral institution. Alternatively, the risks can be partially mitigated by agreeing on applicable law, the seat of arbitration and arbitral institution in jurisdictions which have not imposed sanctions against Russia. While these measures will not block the application of the amendments, they might make it more difficult for a party to argue that access to justice is impeded due to the sanctions.

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References

?1 Federal Law No. 171-FZ dated 8 June 2020, introducing the amendments (text in Russian).

?2 Article 91 of the Russian Commercial (Arbitrazh) Procedure Code.

?3 Judgment of the Commercial (Arbitrazh) Court of Cassation of Moscow District dated 06.07.2020 in case ?40-149566/2019 (text in Russian).

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