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Russian Courts Claim Exclusive Jurisdiction Over Disputes Between Russian-Domiciled Companies: Another Blow to International Arbitration

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Just over 4 months after its previous landmark ruling of 26 July 2024, the Russian Supreme Court continues its crusade against "hostile" or "unfriendly" arbitration forums under the so-called Lugovoy Law (Articles 248.1 and 248.2 of the Russian Arbitrazh (commercial) procedure code). On 28 November 2024, the Supreme Court issued a new ruling in which it held that Russian arbitrazh (commercial) courts can have exclusive jurisdiction over disputes between two companies domiciled in Russia, overriding any arbitration agreement between them (the "Ruling").

Background

1. The Case at Hand

JSC NS Bank ("NS Bank") holds bonds issued by LUKOIL Securities B.V. The bond prospectus included an arbitration clause stipulating that all disputes, including non-contractual ones, would be governed by English law and resolved under the auspices of the London Court of International Arbitration ("LCIA"), and the seat of arbitration would be London.

On 6 May 2022, LUKOIL Securities B.V. paid a coupon rate of USD 19,375 intended for NS Bank under the bonds. This amount was credited to the Russian depository—JSC National Settlement Depository ("NSD"), which was later sanctioned by the EU in June 2022, preventing NS Bank from receiving the funds.

NS Bank filed a claim with the Moscow City Arbitrazh Court against PJSC Lukoil ("Lukoil"), as guarantor of the bonds, for repayment of the coupon. NS Bank argued that the arbitration clause should be disregarded in favour of the exclusive jurisdiction of the Russian courts because the "hostile" countries had imposed sanctions on Russia and its nationals.

Lukoil filed a motion to dismiss NS Bank's claim, citing the arbitration clause. The lower courts,

from first instance to cassation, sided with Lukoil (*see* 1, 2, and 3), and dismissed the claim because, *inter alia*:

- The bond prospectus contained a valid arbitration agreement;
- Russian arbitrazh courts did not have exclusive jurisdiction over the dispute, as the parties to the dispute were Russian entities not subject to sanctions.

NS Bank appealed to the Russian Supreme Court (the "Court") to overturn these decisions.

2. The Lugovoy Law and Further Restrictions

Both the legal basis for transferring the case to the Supreme Court and the Court's ruling align with the development of the Lugovoy Law practice. This notorious law allows Russian courts to assert exclusive jurisdiction over cases involving sanctioned entities and grant injunctions against foreign arbitration or litigation. The *Uraltransmash v. Pesa* case, previously discussed here, set a precedent: the presence of personal sanctions imposed over a plaintiff alone triggers the application of the Lugovoy Law with a rebuttable presumption that those sanctions impeded the plaintiff's access to justice abroad.

Despite the courts' stance in *Uraltransmash v. Pesa*, Russian courts have since broadly interpreted the Lugovoy Law, with plaintiffs often claiming it without personal sanctions imposed over them. To tie sanctions to the forum, judges frequently cite the location of an arbitral institution or court and the arbitration seat in the "unfriendly" states as a key factor. This trend is concerning and widespread.

This is not the first case where Russian courts have applied the Lugovoy Law in a dispute between Russian parties. Until recently, however, this has not been approved by the Supreme Court.

The Court's Conclusions

First, the Court emphasised that when a legal relationship involves a foreign element, Russian arbitrazh court should determine in each case if there are legal grounds for its exclusive jurisdiction, to effectively ensure the claimant's constitutional right to judicial protection. This consideration is not new and aligns with the Plenum of the Russian Supreme Court's position of 27 June 2017 No. 23 (*see, e.g.*, paras. 1, 3 & 4).

With reference to this Plenum's position, the Court also clarified that a case involving a foreign element includes not only cases involving foreign persons but also disputes concerning rights *in rem* and over properties located abroad, as well as disputes related to legal facts occurring abroad, particularly those related to tort.

Second, the Court noted that the Lugovoy Law's purpose is to ensure Russian parties' constitutional right to judicial protection when the restoration of rights, that had been infringed

abroad, becomes impossible or significantly difficult.

The Court ruled that a dispute falls under exclusive competence of Russian courts in particular if:

- the restrictive measures imposed on Russian persons are "the direct cause of the dispute," or
- the arbitration agreement became unenforceable in accordance with intent that the parties had had when entering into the agreement "due to the emergence of obvious obstacles to access to justice" for one of the parties.

Third, if the dispute has arisen from restrictive measures by the foreign state where it is to be heard, the local arbitrators (judges) cast doubts as to their impartiality in the eyes of the Court. The Court considers that "a deliberate statement on the legality (lawfulness) of the imposition of restrictive measures" may affect the resolution of the dispute on the merits and violate principles of independence, impartiality, as well as party equality and adversarial procedure.

Lastly, Russian courts may presume obstacles to access to justice when a party experiences hurdles in resolving a dispute abroad in accordance with the terms that the parties initially agreed on. The Court held there should be a substantial and unforeseeable change of circumstances as compared to the time the parties agreed on the dispute resolution clause.

In the Court's view, unreasonable financial, temporal, or reputational costs required to initiate, continue, and complete proceedings do not allow to exercise the constitutional right to judicial protection and place the Russian party in a "deliberately disadvantageous position." This can be caused by various obstacles to accessing justice, including difficulties in paying arbitration or state fees, lack of financial or other ability to hire a foreign representative, and restrictions on physical presence at the place of dispute resolution.

On the basis of the above, the Court concluded that "in case NS Bank applies to LCIA, there is a high probability that a decision to be rendered would correlate with the goals that the sanctioning states are trying to achieve in relation to the financial sector of the Russian economy and its representatives" (the Court also mentioned that later the UK imposed sanctions on NSD—probably in an attempt to link the sanctions to the forum). The dispute stems from the restrictive measures that led to the bank's inability to receive funds. The possibility of the dispute being heard by the LCIA tribunal is "largely hypothetical" for NS Bank, as the associated costs impede their constitutional right to judicial protection, which NS Bank could not have foreseen when acquiring the disputed bonds and consenting to the LCIA clause.

The Supreme Court overturned the lower courts' decisions and remanded the case to the first instance court. The Moscow Arbitrazh (Commercial) court will review the case in due course, but the Supreme Court's decision will have immediate effects on other cases.

Implications of the Ruling

This Ruling advances a worrying trend of Russian courts rejecting foreign arbitral proceedings in

case there is a connection to sanctions. This case is notable because it involves two Russian entities that are not under personal sanctions and validates the trends of applying the Lugovoy Law beyond its express wording.

Following this approach, any unforeseeable difficulties or costs in arranging international arbitration can invalidate dispute resolution clauses. The Court declared that international arbitration under LCIA rules would not be independent and impartial due to sanctions (this is likely to apply to proceedings under other rules as well). In doing so, the Court implied its stance from a previous ruling that foreign ("unfriendly") arbitrators and institutions are presumptively non-independent and non-impartial, without clarifying how to rebut this presumption. In these conclusions, the Court did not differentiate between the foreign courts and foreign-seated arbitrations, regardless of tribunal composition.

Importantly, the Court reasoned its approach by mentioning, *inter alia*, that the Russian parties seeking satisfaction from guarantors can be considered by arbitrators of a sanctioning state as a circumvention of EU sanctions. Relatedly, the Court of Justice of the EU was recently requested by the Swedish court to provide its interpretation of the Article 11 of the EU Regulation 833/2014. Its ruling will cast a light on whether the Russian Supreme Court, on a whim, was right in its conclusions, at least when it comes to an EU-seated arbitration with sanctioned parties from Russia.

Although the case involved two Russian companies, the Court's authoritative position will likely extend to all the other cases with the parties that are potentially subject to the Lugovoy Law, dragging their opponents to Russian courts.

The positive aspect of the Ruling might be that the Court did not accept that merely submitting a request to transfer a case to Russian courts suffices to apply Lugovoy Law. Evidence to support such a motion shall be provided.

For the time being, the authors suggest taking into account the following important points when dealing with such disputes:

1. To the extent possible, it can be helpful to amend existing arbitration agreements to refer disputes with Russian parties to *ad hoc* arbitration or arbitration under the rules of institutions in "Russia-friendly" states (consider arbitrateAD, DIAC, ISTAC, and such) and choose seats outside "unfriendly" countries list.
2. The Court's position may be interpreted as protecting arbitration agreements where the difficulties in arranging representation and making payments were foreseeable at the time the agreement was entered into. However, given the general trend, if any new arbitration agreement is to be drafted, it makes sense to avoid the "standard" arbitration institutions (such as the SCC or ICC) and seats in Western countries.
3. We can also reiterate our conclusion that today it is more than necessary, when appointing arbitrators, to duly investigate their background, the statements they have made publicly, their nationality or residence, and other accessible information that can show their partiality in the eyes of Russian courts.

Conclusion

This Russian Supreme Court's ruling reflects a growing scepticism towards foreign arbitral institutions, particularly those in "unfriendly" states. The Court has signalled a further move towards the primacy of national jurisdiction amid international sanctions, complicating relations between foreign companies and Russian counterparties and potentially discouraging new connections. It also poses new challenges for dispute resolution lawyers.

Historically, international arbitration has served as a neutral tool for resolving disputes despite political tensions and armed conflicts. The Supreme Court's Ruling—as another response to or trigger of Russia-unfriendly states—further reduces a chance of widespread peaceful dispute resolution proceedings involving Russian entities. This stance discourages foreign companies, even from Russia-friendly states, from engaging with Russian counterparties, signalling a red flag in due diligence and increasing transactional costs for all Russian companies, including entirely private and not sanctioned ones.

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