ARBITRATION REFORM AND STATE COURT MERGER IN RUSSIA

Christoph Harler and **Evgen Antipin** of **WilmerHale** give a status update on how international arbitration is being impacted by local reforms to arbitration laws and the country's state court system

Russia is currently reforming its domestic and international arbitration laws. Further, Russia merged the supreme courts of the civil and commercial jurisdictions in a reform of the state court system. Though, at first sight, the reform is not arbitration-related, this second reform could affect international arbitration significantly.

While the proposed arbitration reform is not complete, and the draft laws might still change, the state court reform came into effect in August 2014. This article highlights some of the expected main elements of the arbitration reform, in particular their relevance to international commercial arbitration. Furthermore, a year after the state court reform, we look at the developments from the state court merger, as far as they impact international commercial arbitration.

Background

According to the explanatory note to the draft arbitration laws, the purpose of the arbitration reform is to promote arbitration within Russia, to eliminate opportunities for misuse of arbitration proceedings and to reduce the caseloads of the state courts.

The legal framework in Russia differs for domestic arbitration and international arbitration. The law governing domestic arbitration was adopted in 2002, but did not implement many of the provisions of the 1985 UNCITRAL Model Law on International Commercial Arbitration (1985), which many saw as a problem with the law.

The law governing international commercial arbitration was adopted in 1993 and closely followed the 1985 UNCITRAL Model Law. After the UNCITRAL Model Law was amended in 2006, discussions arose to adapt the Russian law on international commercial arbitration.

Under the proposed arbitration reform, Russia will not consolidate its arbitration laws into a common legal framework for all arbitration proceedings, but will maintain the two separate regimes for domestic and international arbitrations.

According to the explanatory note to the state court merger law, the purpose of the merger is to avoid contradictory last instance civil law judgments.

The Russian state court system provides for two parallel civil jurisdictions – one for common civil cases, and the other for commercial matters. The term for the commercial courts is 'arbitrazh' courts (which has nothing to do with arbitration). Until as recently as August 2014, Russia's Supreme Arbitrazh Court (SAC) was the last instance in commercial disputes, while the Supreme Court of the Russian Federation (Supreme Court) was the last instance for (other) civil cases as well as for criminal, administrative ▶

and tax matters. The recognition and enforcement of foreign arbitral awards used to be in the realm of the SAC (as the last instance).

Under the reform, the SAC was merged into the Supreme Court, which thereby assumed the SAC's function to become the final instance for the recognition and enforcement of foreign arbitral awards. Below the Supreme Court level, common civil and commercial (arbitrazh) jurisdictions were not merged.

Authorisation requirements for arbitral institutions

One of the main goals of the arbitration reform is to fight 'pocket arbitrations', and 'fraudulent arbitrations'. In short, pocket arbitration refers to a situation where a dispute is resolved under the auspice of an arbitral institution, which is co-founded by one of the parties, and which therefore lacks independence and/or impartiality. Fraudulent arbitration more generally comprises any arbitral award that has been rendered under the auspice of an arbitral institution that administered the case with a fraudulent intent.

Under the proposed reform, domestic and foreign arbitral institutions will need to obtain state authorisation to hold Russian-seated proceedings. The draft further contains transparency requirements for arbitral institutions, such as requirements to publish online the lists of their founders, and of at least 30 qualified arbitrators. Without an official authorisation, arbitral institutions will no longer be allowed to conduct arbitration proceedings seated in Russia.

It is difficult to assess this part of the reform before the practical effects can be observed. Prima facie, the authorisation requirement on the one hand might be a suitable means to provide for more transparency over the arbitration institutions and to reduce fraudulent and pocket arbitrations. On the other hand, state control over arbitral institutions is generally considered as adverse for arbitration proceedings, in particular from an international arbitration perspective.

Further, arbitration reforms in Latvia and Ukraine, which introduced similar authorisation requirements, did not eliminate fraudulent and pocket arbitrations. Moreover, ad hoc arbitrations may be used to circumvent state authorisation and to continue the phenomenon of fraudulent arbitrations.

In any event, awards issued as a result of packet arbitration tribunals would not be unenforcable as a result of these reforms. Arbitrations administered by a party-affiliated institution are biased. In these circumstances it may nevertheless be very difficult, if not impossible, to prove to a state court (that decides about setting aside/enforcing the award) that the tribunal was impartial, or if the process has been unfair.

For these reasons, the former SAC held in the context of domestic arbitration that the mere participation of the co-founders of arbitral institutions rendered an award unenforceable because it infringes the Russian public policy. Contrary to this jurisprudence, the Constitutional Court held that the participation of a co-founder was in line with the Russian constitution and implied that it was up to the legislature to change the law. The proposed arbitration reform does not implement this change, however.

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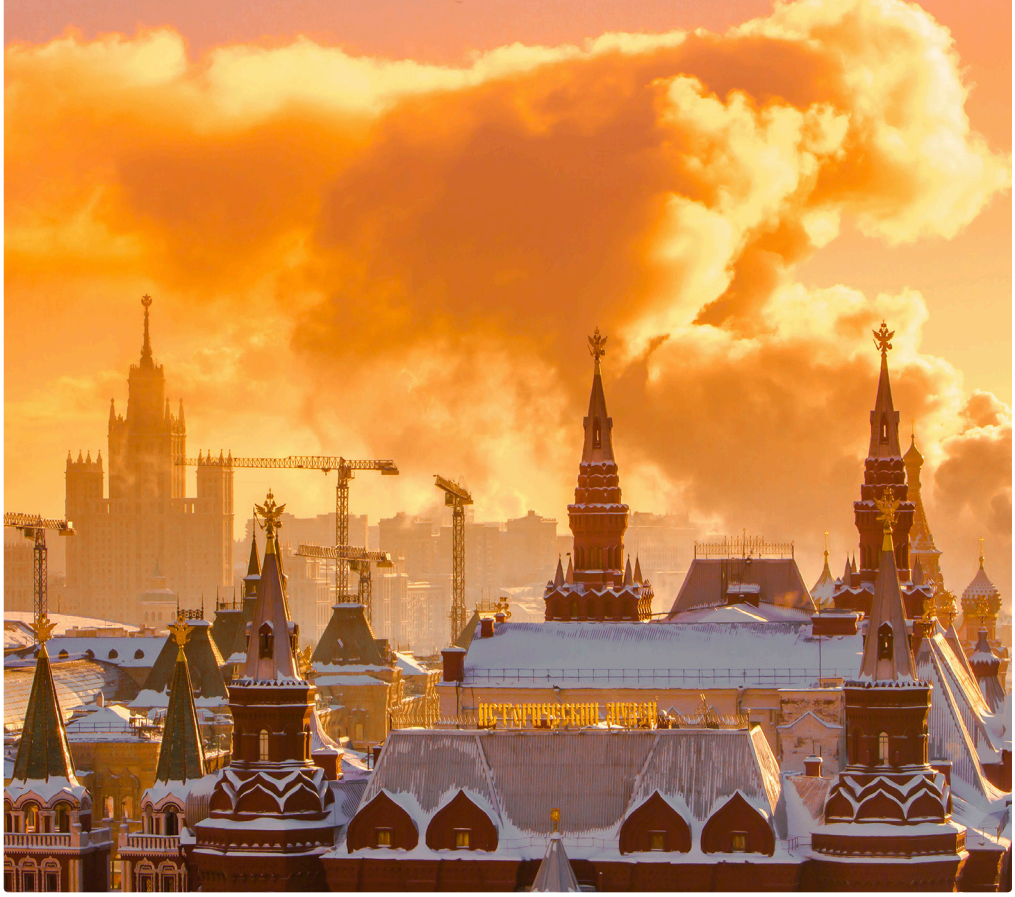
Arbitrability of corporate disputes

According to recent Russian jurisprudence, corporate disputes cannot be brought under arbitration proceedings. This not only applies to matters relating to corporate rights themselves (e.g. incorporation of a company; transfer of shares), but also comprises contractual obligations in connection with corporate rights (e.g. guarantee or payment claims under share purchase agreements).

In this regard, the proposed reform is supportive of arbitration. It introduces categories of corporate disputes (including M&A disputes) that will be arbitrable in institutional arbitration proceedings (not in ad hoc arbitrations). In the cases explicitly mentioned by the draft, the arbitration for such corporate disputes has to be seated in Russia and arbitral institutions must have a specific set of rules for corporate disputes.

While this development has created opportunity to resolve some corporate disputes under arbitration, the draft law is not entirely clear in a number of points, and it remains to be seen



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how Russian courts will construe and apply the new laws.

Arbitration agreements

The proposed reform of the arbitration laws also addresses the definition of an arbitration agreement. First, the draft adjusts the definition of an 'arbitration agreement' to the wording of the 2006 UNCITRAL Model Law. Second, the draft provides that arbitration clauses can be contained in the statutes of a company. This however does not apply to public joint stock companies and companies having more than 1000 shareholders with voting rights. Third, the draft includes a number of additional provisions intended to facilitate arbitration and to protect arbitration clauses from state court interference. Perhaps most significantly, doubts regarding the validity of arbitration clauses shall be interpreted in favour of their validity.

Arbitration proceedings

In the current Russian law on domestic arbitration, there are a number of essential features of assistance by state courts to arbitral tribunals that are missing. The proposed reform would close this gap and for example, introduce state court support in obtaining evidence. For international arbitration, such mechanisms are already in place.

There is one proposed change that might turn out to be problematic for international arbitration. Currently, when the parties cannot agree, and an institutional default mechanism is absent, the president of the Chamber of Commerce of the Russian Federation will appoint an arbitrator. According to the draft, the state courts will assume this function.

Unlike the current approach, which relies on the president of the Chamber of Commerce to be familiar with parties' expectations in international arbitration, and to have a list of potentially suitable arbitrators, the approach after the reform will rely on state court judges to make appointments. Those judges may have little or no experience with international arbitration, or in appointing suitable arbitrators. Moreover, state court judges will play this role in addition ▶

UNDER THE PROPOSED REFORM, DOMESTIC AND FOREIGN ARBITRAL INSTITUTIONS WILL NEED TO OBTAIN STATE AUTHORISATION TO HOLD RUSSIAN-SEATED PROCEEDINGS

- to their existing caseload. This part of the reform therefore may result in less suitable arbitrators being appointed, and may also delay the arbitration process.

Setting aside, recognition and enforcement of awards

Russia's current international arbitration law already provides for the recognition and enforcement of foreign arbitral awards. Denial of recognition and enforcement is limited to the grounds contained in the New York Convention 1958. However, Russian courts have been criticised for too frequently refusing to enforce foreign arbitral awards under the guise of public policy. While public policy is not defined under Russian law, some Russian courts have interpreted the public policy exception in the New York Convention broadly to refuse to enforce awards against Russian parties.

By issuing 'information letters' in 2005 and 2013, the SAC took steps to address this matter and to provide a narrower interpretation of public policy and other grounds for refusing recognition and enforcement. The title 'information letter' is misleading; such letters provide strong guidance for lower courts, which usually comply with them (knowing that they otherwise run the risk of being overturned).

According to practitioners, the SAC has areputation for having been the most progressive Russian court, particularly because of its supportive approach towards international arbitration. From an arbitration perspective, one of the concerns regarding the state court merger therefore was that the Supreme Court might depart from the course the SAC had taken, and implement a less arbitration-friendly jurisprudence. These concerns have so far not materialised. The Supreme Court has expressly referred to the SAC's 2013 information letter, and thus shared its narrow interpretation of public policy. It appears that the Supreme Court has also confirmed other recent arbitration-related case law by the SAC in its decisions following the state court merger.

There is, however, one apparent downside of the merger for international arbitration. Before August 2014, the recognition and enforcement process for foreign arbitral awards comprised up to three instances, with the SAC as final instance. The last instance review by the Supreme Court is two-fold. Each of the two Supreme Court instances may take more time than the one-stage final SAC review. This means that following the merger, recognition and enforcement of foreign arbitral awards may take more time.

Another feature of the proposed arbitration reform is the recognition of foreign declaratory awards. According to the draft, declaratory foreign arbitral awards shall be recognised automatically, and without any further formalities, if international treaties and the law allow for their recognition. The encumbered party will have to proactively file an objection against such a declaratory award. Still, entries to public registers continue to require confirming state court decisions. That means that declaratory arbitral awards aiming for such registration continue to be subject to state court control.

Finally, the draft law for international arbitration allows the parties to waive their right to set aside the arbitral award, as under the similar provisions contained in Swiss, Belgian, French and Swedish laws.

Summary

It is too early to assess the reforms on their merits. The proposed arbitration law reform certainly could have gone further. With regard to the state court merger reform, it appears that the Supreme Court continues the arbitration supportive course of the SAC. It remains to be seen in future decisions whether this is a stable trend. ■

About the authors

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