Substantive Public Policy Concept in Enforcement of Foreign Arbitral Awards in Russia

Author: Shtromberg, Alexandra  
014593781  
Supervisor: Ville Pönkä  
Degree: International Master’s Degree Programme in International Business Law  
Date: 18.04.2017
### Abstract

Predictability in the enforcement of foreign arbitral awards is crucially important both for the parties to a certain dispute and the state where enforcement is sought. Being arbitration-friendly means increasing of investment attractiveness. For parties, it means that their contractual will regarding arbitration is respected and party autonomy is in no way breached.

In practice, the Russian Federation is still an unknown playing field for those parties who aim to enforce foreign arbitral awards and file respective claims with the Russian commercial courts. The Russian Federation is the party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, meaning that enforcement courts rely on the narrow scope of grounds to refuse recognition and enforcement of foreign arbitral awards. In practice, Russian commercial courts tend to interpret provisions of the Convention incoherently. One of such examples is the wide interpretation of public policy exception that allows to refuse recognition and enforcement of foreign arbitral awards in cases when such would be contrary to the public policy of that country.

The thesis explores the risks that parties face when the interested party or the court itself brings public policy to the light. It analyses the modern concept of public policy under Russian law and court practice and examines the enforcement trends regarding public policy exception.

### Keywords

- Public policy
- International public policy
- International commercial arbitration
- Recognition
- Enforcement
- Russian law
- New York Convention

### Where deposited

University of Helsinki, Faculty of Law

### Additional information
# TABLE OF CONTENTS

**SOURCES** ................................................................................................................................. iii  
International materials .................................................................................................................. iii  
Constitutions, legal codes & legislation ......................................................................................... iii  
Cases cited ........................................................................................................................................ iv  
Scholarly material ............................................................................................................................ v  

**ABBREVIATIONS** ....................................................................................................................... xvi

## 1. INTRODUCTION .......................................................................................................................... 1  
1.1. Role of recognition and enforcement of foreign arbitral awards and current situation in the Russian Federation .......................................................................................................................... 1  
1.2. Research subject and research questions .................................................................................. 3  
1.3. Structure of the research .......................................................................................................... 4

## 2. PUBLIC POLICY IN INTERNATIONAL COMMERCIAL ARBITRATION ........ 4

2.1. General principles of recognising and enforcing foreign arbitral awards in the international landscape .......................................................................................................................... 4  
2.2. Definition of public policy ...................................................................................................... 6  
2.3. International regulatory framework of public policy ............................................................... 9  
2.4. Applying public policy under the New York Convention ....................................................... 11  
2.5. Role and impact of public policy ............................................................................................ 14  
  2.5.1. Impact on legal systems ..................................................................................................... 14  
  2.5.2. Stakeholder analysis .......................................................................................................... 15  
  2.5.3. Impact on courts ............................................................................................................... 15  
  2.5.4. Impact on parties ............................................................................................................... 16  
  2.5.5. Impact on arbitral tribunals ............................................................................................... 17  
2.6. Classifications of public policy ............................................................................................... 17  
2.7. Public policy versus other grounds ........................................................................................ 22  
2.8. Conclusions: roadmap to analyse national public policy ......................................................... 24

## 3. PUBLIC POLICY IN RUSSIA ...................................................................................................... 25

3.1. Introduction ............................................................................................................................... 25  
3.2. Emergence of public policy in Russian legal theory ............................................................... 25  
3.3. Mentality of stakeholders in enforcement of foreign arbitral awards .................................... 27  
  3.3.1. Mentality of the enforcement courts ................................................................................ 28  
  3.3.2. Mentality of the parties to the dispute ............................................................................ 29  
3.4. Current framework of public policy in Russia ......................................................................... 30  
  3.4.1. Legislation ....................................................................................................................... 30  
  3.4.2. Role of the Supreme Commercial Court (2002-2014) in forming concept of substantive public policy ........................................................................................................... 32
4. SUBSTANTIVE PUBLIC POLICY IN PRACTICE .................................................. 34
4.1. Introduction ........................................................................................................ 34
4.2. Procedure of recognition and enforcement of foreign arbitral awards under Russian law . 35
4.3. Applicable principles of Russian law .................................................................. 39
4.4. Case studies: introductory notes ......................................................................... 44
4.5. Illegality of underlying transactions .................................................................... 46
4.6. Proportionality of liability .................................................................................. 53
4.7. Violation of branch legislation and public policy as a result of enforcement .......... 59
   4.7.1. Currency control .......................................................................................... 59
   4.7.2. Bankruptcy law ........................................................................................... 60
   4.7.3. Principles of procedural law ......................................................................... 61
   4.7.4. Property law ............................................................................................... 61
4.8. Scope and capacity of parties involved ............................................................... 62
4.9. Mala fide of parties referring to violation of substantive public policy ............... 66
4.10. Conclusions ....................................................................................................... 68

5. CONCLUSIONS ...................................................................................................... 68
SOURCES

International materials

International Conventions & Treaties

1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965 Washington Convention)
1972 Convention on the settlement by arbitration of civil law disputes resulting from relations of economic and scientific-technical cooperation (1972 Moscow Convention)
1975 Inter-American Convention on International Commercial Arbitration (Panama Convention)

Model Legislation & Guidelines

IBA REPORT

ILA REPORT, ILA RECOMMENDATIONS
International law association, comm. on int’l commercial arb., Final report on public policy as a bar to enforcement of international arbitral awards (2002).

UNCITRAL Model Law

Constitutions, legal codes & legislation

Civil Code of the Russian Federation (Гражданский кодекс Российской Федерации)
Civil procedure code of the Russian Federation (Гражданский процессуальный кодекс Российской Федерации)
Commercial procedural code of the Russian Federation (Арбитражный процессуальный кодекс Российской Федерации)
Constitution of the Russian Federation (Конституция Российской Федерации)


Law of the Russian Federation No. 5338-1 dated 7 July 1993 “On international commercial arbitration” (Закон Российской Федерации от 07.07.1993 №5338-1 «О международном коммерческом арбитраже»)


**Cases cited**

**Russian cases**

Adecco AG v OOO Orglot
Apaucuck Point Environmental Limited v OAO Rosgazifikatsiya
Baltiysky Zavod v Stena RoRo
Ciments Francais v OJSC Holding Company Sibirsky Tsement
Connyland AG v OOO Mir-disain
Consulting, Management & Contracting Co. v Sylovye Mashiny
Energo-Management Anstalt vs Proizvodstvennoye obyedineniye Teplovodokanal
Euro-Asian Investment Corporation v OAO Primorkhlebproduct (PMK)
Falkland Investments Ltd. v VBTRF OAO
Federalevel Holdings Ltd. v Ishchuk
Fringilla Co. Ltd. v OOO Rybprominvest
Gartic Limited v OOO Obyedinennaya sudstroitelnaya kompaniya
Hipp GmbH & Co. Export KG v OOO Sivma Detskoe Pitanie
ING Bank N.V., London Branch v OJSC Holding Company Sibirsky Tsement
International Finance B.V. v OAO AB Inkombank
Joy-Lud Distributors International Inc. v JSC Moscow Oi Refinery
Kruken GmbH v Avtodor-Agro
Lugana Handelsgesellschaft GmbH v OAO Ryazansky zavod metallokermischeskikh priborov
NANA offshore v ZAO Trast-oil
OAO Bank VTB v OAO Finansovaya lizingovaya kompaniya
Odjfell SE v OJSC Sevmash
Oil & Natural Gas Corporation v OJSC Amur
Omegatech Electronic GmbH v state factory Izmeritel
OOO Remontno-proizvodstvennoye obyedineniye v OAO RZD
United World v Krasny Yakor
Sokofl Star Shipping Co. Inc. v Technopromexport
Stena RoRo v Baltiysky Zavod
Traviata Environmental Ltd. v OAO Rosgazifikatsiya
Ukrainian Confectionery Factory A.V.K. v AVK-“Yug”
Yukos Capital S.A.R.L. v OAO Tomskneft
OOO Cable and Wireless SNG Svyaz v ZAO Zebra Telekom

Foreign cases

DST v Rakoil
Mitsubishi Motors Corp. v. Sole Chrysler-Plymouth

Scholarly material

NB. Some Russian sources do not have indication of page numbering as they have been accessed through ConsultantPlus database where electronic articles do not have page numbering.

Antonov  

Asoskov  

Astakhova  

Baker & McKenzie  

Baker et al.  

Blackaby et al.  
Nigel Blackaby, Constantine Partasides, et al., Redfern and Hunter on International Arbitration (sixth edition, OUP 2015)

Böckstiegel  

Bogatina  
Julia Bogatina, Оговорка о публичном порядке в международном частном праве: теоретические проблемы и современная практика (Public policy exception in international private law: theoretical problems and modern practice) (Statut, 2010)

Born 2001  

Born 2014  

Born 2015  


Davydenko & Khizunova  Dmitry Davydenko, and Alexandra Khizunova, “Значение и функции оговорки о публичном порядке в иностранном и российском праве” (Meaning and function of public policy exception in foreign and Russian law) [2013] 2 Zakon.


<table>
<thead>
<tr>
<th>Author</th>
<th>Title and Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Karabelnikov 2006</td>
<td>Boris Karabelnikov, “Высший арбитражный Суд РФ поддерживает внутренние третейские суды, но не доверяет международному арбитражу” (The Supreme Commercial Court of the Russian Federation supports the internal arbitral tribunals but does not trust international commercial arbitraion) (Consultant Plus, 2006)</td>
</tr>
<tr>
<td>Karabelnikov 2008</td>
<td>Boris Karabelnikov, “Исполнение и оспаривание решений международных коммерческих арбитражей. Комментарий к Нью-Йоркской конвенции 1958 г. и главам 30 и 31 АПК РФ 2002 г.”</td>
</tr>
</tbody>
</table>
(Enforcement and disputing the awards of international arbitral tribunals. Commentary to the 1958 New York Convention and chapters 30 and 31 of the Commercial Procedural Code of the Russian Federation) (Statut, 2008)


strengthenes creditors right to challenge enforcement decisions accessed 31 March 2017

Kozmenko & Boog

Kronke et al.

Kulkov
Maxim Kulkov, Enforcement of International Arbitral Awards in Russia, ABA Teleconference Handout (American Bar Association, 17 November 2009) <http://www.americanbar.org/content/dam/aba/multimedia/international_law/docs/committees/russia_eurasia/enforcingarbitrationawardsinrussiaandukraineclematerials.authcheckdam.pdf> accessed 8 March 2017

Kurochkin 2008
Sergey Kurochkin, Государственные суды в третейском разбирательстве и международном коммерческом арбитраже (State courts in the commercial arbitration and international commercial arbitration) (Wolters Kluwer, 2008)

Kurochkin 2013
Sergey Kurochkin, “Нарушение публичного порядка Российской Федерации как основание для отказа в признании и приведении в исполнение иностранных судебных и арбитражных решений” (Violation of public policy of the Russian Federation as the ground to refuse recognition and enforcement of foreign judgments and arbitral awards) [2013] 2 Zakon.

Kurzinsky-Singer

Lalive

Lanier & Dolinar

Lew et al.

Liebscher
Lopatin

Ma

Magnusson

Maurer
Anton Maurer, Public Policy Exception Under The New York Convention: History, Interpretation, and Application

Micielwrath & Savage

Melnikov & Teselkin

Minina

Moedritzer & Whittaker
Mark Moedritzer and Kay C Whittaker, Enforcement of Foreign Judgments in 28 jurisdictions worldwide (Law Business Research Ltd 2011)

Morozova
Julia Morozova, К вопросу об отказе в признании и приведении в исполнение иностранных судебных и арбитражных решений (On refusal to recognise and enforce foreign judgments and foreign arbitral awards) (SPS Konsultant, 2015)

Muranov
Aleksandr Muranov, “Некоторые аспекты понятия "публичный порядок" применительно к международному коммерческому арбитражу в России” (Some aspects of public policy concept in the framework of international commercial arbitration in Russia) [2001] 5 Mezhdunarodnoye pravo 396.

Murphy

Neshatayeva Tatyana Neshatayeva, Международное частное право и международный гражданский процесс (Private international law and international civil procedure) (Gorodets, 2004)


Opalev Rim Opalev, Оценочные понятия в арбитражном и гражданском процессуальном праве (Evaluative definitions in arbitration and civil proceedings) (Wolters Kluwer, 2008)


Pavlova Natalya Pavlova, “Оговорка о публичном порядке как судебный эксклюзив и предел вежливости конкретной нации. Комментарий к Обзору практики рассмотрения арбитражными судами дел о применении оговорки о публичном порядке” (Public policy exception as a judicial exclusive and the limit to the principle of comity of nations. Commentary to
the case law review regarding implementation of public policy exception by state commercial courts) [2013] 7 Vestnik VAS RF.

**Pellew**
Dominic Pellew, Russian Federation: Recognition And Enforcement Of Foreign Arbitral Awards In Russia (Mondaq, 8 January 2002) <http://www.mondaq.com/x/15098/Recognition+And+Enforcement+Of+Foreign+Arbitral+Awards+In+Russia> accessed 8 March 2017

**Ponty**

**Poon**

**Pryles**

**Rachkov**
Ilia Rachkov, “Russia’s Supreme Arbitrazh Court Summarizes Application of the Public Policy Clause” (King & Spalding, 6 August 2013) <http://www.kslaw.com/imageserver/KSPublic/library/publication/ca080613.pdf> accessed 7 March 2017

**Raschevsky et al.**

**Rothstein**
Daniel Rothstein, “An Introduction to Enforcement in Russia of Foreign Arbitral Awards, and Barriers to Entry to American Courts” in Russia/Eurasia Committee Newsletter of the Section of International Law of ABA, Spring (2009).

**Sadikov**
Oleg Sadikov, “Императивные нормы в международном частном праве” (Imperative norms in private international law) [1992] 2 Moskovskij zhurnal mezhdunarodnogo chastiogo prava 82.

**Shinyayeva**

**Skvortsov & Yarkov**
Oleg Skvortsov, Oleg Yarkov, “Комментарий к Федеральному закону "О третейских судах” (Commentary to the Federal law On the arbitration courts) [2003] 4 Treteiskiy sud.

**Smit**

**Spiegelberger**

**Statistics 2013**
Аналитическая записка к статистическому отчету о работе арбитражных судов в Российской Федерации в 2013 году (Analytical note to the statistical
report on the work of commercial courts in the Russian Federation in year 2013) (Arbitr.ru) 

Storozhkova

Elena Storozhkova, “Основополагающие принципы российского права в правовой доктрине” (Fundamental principles of the Russian law in legal doctrine) [2012] I Simbirskij nauchnyj vestnik

Tapola 2005


Tapola

Diana Tapola, “Enforcement of Foreign Judgments and Awards in Commercial Matters in Russia” (Doctoral thesis, University of Helsinki 2015)

Tarasov

Igor Tarasov, “Основополагающие принципы российского права и публичный порядок: Проблемы разграничения” (Fundamental principles of Russian law and public policy: problems of distinction) [2007] 10 Arbitrazhnyj i grazhdanskij process 22.

Terez


Traspov 2003

Roman Traspov, “Международный коммерческий арбитраж: оговорка о публичном порядке как основание отказа в признании или приведении в исполнение иностранных арбитражных (третейских) решений” (International commercial arbitration: public policy exception as a refusal to recognise and enforce foreign arbitral awards) [2003] 6 Arbitrazhnyj i grazhdanskij process

Usoskin


Van der Berg


Van der Berg 2011


Van der Berg 2012

<table>
<thead>
<tr>
<th>Author</th>
<th>Title and Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zaitsev</td>
<td>Alexey Zaitsev, “Комментарий к гл. 46 ГПК РФ &quot;Производство по делам об оспаривании решений третейских судов&quot; (Commentary to the Chapter 46 of the Civil Procedure Code” on disputing foreign awards) [2003] 5(29) Tretezskiy sud.</td>
</tr>
<tr>
<td>Zhiltsov</td>
<td>Alexey Zhiltsov, “Оспаривание решений международных коммерческих арбитражей в соответствии с российским законодательством - современные тенденции” (Disputing foreign arbitral awards in accordance with the Russian legislation) in Mezhdunarodnyj kommercheskij arbitrazh: sovremennye problemy i reshenija: Sbornik statej k 75-letiju Mezhdunarodnogo kommercheskogo arbitrazhnogo suda pri Torgovopromyshlennoj palate Rossijskoj Federacii (Statut, 2007)</td>
</tr>
</tbody>
</table>
**ABBREVIATIONS**

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>CPC</td>
<td>The Commercial Procedure Code of the Russian Federation</td>
</tr>
<tr>
<td>IBA Report</td>
<td>IBA subcommittee on recognition and enforcement of arbitral awards: Report on the Public Policy Exception in the New York Convention</td>
</tr>
<tr>
<td>IBA Report</td>
<td>Final Report on Public Policy as a Bar to Enforcement of International Arbitral Awards</td>
</tr>
<tr>
<td>NYC</td>
<td>Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the &quot;New York Convention&quot;)</td>
</tr>
<tr>
<td>OAO</td>
<td>Open Joint Stock Company (in Russian)</td>
</tr>
<tr>
<td>OOO</td>
<td>Limited Liability Company (in Russian)</td>
</tr>
<tr>
<td>SCC</td>
<td>Supreme Commercial Court of the Russian Federation</td>
</tr>
<tr>
<td>SCC Presidium</td>
<td>Presidium of the Supreme Commercial Court of the Russian Federation</td>
</tr>
<tr>
<td>ZAO</td>
<td>Closed Joint Stock Company (in Russian)</td>
</tr>
</tbody>
</table>
1. INTRODUCTION

1.1. Role of recognition and enforcement of foreign arbitral awards and current situation in the Russian Federation

The parties draft an agreement and include an arbitration clause in order to ensure the predictability of dispute resolution mechanism. Then something goes wrong (for instance, one of the parties fails to perform delivery), and the suffering party initiates the arbitration proceedings. The arbitral tribunal issues an arbitral award. This makes the party happy and content that its rights are restored. However, getting decision on paper is not enough. The award shall be enforced enabling a suffering party to get material results. Suddenly, it turns out that the assets of the debtor are located in Russia. The party initiates the enforcement proceedings being sure that in a couple of months local bailiffs will complete the enforcement. Then the Russian state court (enforcement court) rules that it refuses to enforce a foreign arbitral award as its enforcement is contrary to public policy under the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention, the NYC) and applicable Russian legislation.

The description above illustrates an abstract situation when interpretation of public policy exception may become a stumbling block to restoring a contractual balance. It is almost impossible to predict exactly how the Russian courts will interpret the public policy as a ground to refuse enforcement of a foreign arbitral award. Russian state courts interpret public policy exception widely, refusing enforcement in circumstances that theorists and practitioners outside Russia may find shocking.¹ This stems inter alia from the lack of thorough theoretical research on this subject. The last thorough Russian monography on the issues of public policy in private international law was Brun's “Public policy in private international law”, published back in 1916.² Now, there is a growing amount of research on this subject. However, rapid changes into the Russian substantive and procedural legislation make it difficult for research to keep up to date.

The state court should not play a role of cassation court (the court that reviews the case on the merits) in relation to a foreign arbitral tribunal when deciding whether to refuse enforcement of

¹ Baker p.7
² Bogatina
foreign arbitral awards.\textsuperscript{3} However, in practice, Russian state courts broadly assess public policy as a ground to refuse to recognise and enforce foreign arbitral awards under the NYC. Although Russian national legislation meets international standards on its face, the practical application of it by Russian courts has been widely criticised, especially with regard to award enforcement.\textsuperscript{4} Namely, the unpredictably wide interpretation of the public policy exception in Russian is hardly in harmony with the trends of narrow interpretation of public policy in other states.\textsuperscript{5} It becomes difficult for the foreign parties to structure transactions and resolve disputes without triggering a rejection for recognition and enforcement based on public policy.\textsuperscript{6} Although courts rarely refuse enforcement in the end, the smoothness of the road to this result is another issue.\textsuperscript{7} In light of this, the status of a public policy as a stumbling block for the smooth development of international transactions highlights actuality of the research.

Now we can observe some positive trends in enforcement of foreign arbitral awards. The enforcement rate has steadily increased to average rates of 85-89\% in the decade between 2003 and 2013.\textsuperscript{8} This results from the development of relevant Russian legislation, the increasing experience of Russian judges with international arbitration, and the favorable practice of the Supreme Commercial Court of the Russian Federation (the SCC).\textsuperscript{9} In general, foreign business does not actively participate in Russian commercial court proceedings. In 2013, in Russian commercial courts in total there were 2408 cases examined and 765 letters rogatory executed that involved participation of foreign parties. Out of that amount, 132 cases dealt with foreign-trade deals, 6 cases dealt with foreign investments. However, according to official statistics of the SCC, Russian courts have considered few applications for enforcement of foreign judgments and foreign awards: 145 in 2010, 174 in 2011, and 179 in 2012.\textsuperscript{10} In 2015, there were in total 271 claims on recognition and enforcement of foreign arbitral awards and judgements, out of which only 212 were actually examined by the court.\textsuperscript{11} Also, in total, commercial courts examined 132 requests of foreign persons for injunctive measures.\textsuperscript{12} Unfortunately, the enforcement courts (the courts deciding whether to refuse recognition and enforcement of foreign arbitral awards) do not publish statistics on the success rate of enforcement applications and grounds for the enforcement

\textsuperscript{3} Storozhkova p.125
\textsuperscript{4} Baker et al. p. 2
\textsuperscript{5} Wires p. 13
\textsuperscript{6} Field Fisher Waterhouse p.3
\textsuperscript{7} Nikiforov p. 788
\textsuperscript{8} Kozmenko & Bogg
\textsuperscript{9} Kozmenko & Bogg
\textsuperscript{10} Grishchenkova p.450
\textsuperscript{11} Khodyreva
\textsuperscript{12} Statistics 2013

2
of awards.\textsuperscript{13} The lack of coherent and clear statistics deprives the parties of the possibility to evaluate own enforcement risks, and complicates the research on the topic.

Improving records of recognition and enforcement of foreign arbitral awards becomes even more important in light of new political obligations of Russia. Russia became a WTO member in 2012. As part of the “price” of membership, the Russian Federation has undertaken the obligation to open up its markets to broader international competition.\textsuperscript{14} However, in 2015, Russian attractiveness for foreign investors has fallen by 8\%, according to EY.\textsuperscript{15} Russian law and court practice not matching with international standards of arbitration friendliness may be one of the reasons why foreign entities treat the Russian jurisdiction with suspicion.

\textbf{1.2. Research subject and research questions}

The subject of this research is focused on the analysis of application of substantive public policy (substantive public policy) as a ground to refuse enforcement of foreign arbitral awards in recent period (2007-2017). Choosing this time period allows us to analyse how public policy interpretation has been changing under the influence of legislative changes and political factors. This research excludes non-arbitrability that is sometimes addressed under the umbrella of public policy. Research scope is also limited to purely foreign arbitral awards (awards rendered by arbitral institutions located outside Russia), excluding domestic awards that may in some cases fall under definition of “non-domestic” awards under the NYC.

The purpose of this research is to analyse the problems arising from varying interpretation of substantive public policy as a ground for refusal to recognise and enforce foreign arbitral awards in Russia.

The master thesis aims to answer following research questions:

1. What tools does the legal theory provide to effectively analyse national jurisdiction’s approach to interpreting substantive public policy concept?
2. How Russian legal theory, statutory law and case law define substantive public policy exception?
3. How enforcement courts distort interpretation of substantive public policy when applying it in practice?
4. What are the main risks that foreign parties face in the court proceedings on recognition and enforcement of foreign arbitral awards in Russia?

\textsuperscript{13} Pellew
\textsuperscript{14} Antonov p. 317
\textsuperscript{15} EY
1.3. Structure of the research

The research is split into two parts: theoretical and practical. The master thesis begins with the overview of general theoretical understanding of public policy, its features and classifications. This theoretical analysis provides us with the basis for assessing peculiarities of how Russian legal theory generally interprets public policy exception. It also helps to research substantive public policy exception as a ground to refuse to enforce foreign arbitral awards in Russia and reasons why we should prioritise research of substantive public policy when addressing recognition and enforcement of foreign arbitral awards. Theoretical analysis continues with looking into practical specifics of substantive public policy interpretation. The second chapter deals with interpretation and implementation of substantive public policy concept in practice. First, it looks into how peculiarities of procedure of raising substantive public policy influence interpretation of public policy. Secondly, it presents a structured research of different subtypes of substantive public policy as the Russian courts apply them.

Law is like a shaft of a cart, it points wherever you turn it to.

Russian proverb

2. PUBLIC POLICY IN INTERNATIONAL COMMERCIAL ARBITRATION

2.1. General principles of recognising and enforcing foreign arbitral awards in the international landscape

An arbitral award has following characteristics: (a) it results from an arbitration agreement; (b) it has certain minimal characteristics inherent in the concept of an “award”; and (c) it resolves a substantive issue. Arbitral awards finally determine questions of substance and competence submitted to the arbitration and in limited number of cases, resolve some procedural issues. If these conditions are not met, the decision rendered by an arbitral tribunal will not be subject to the pro-arbitration regime under international treaties and national arbitration legislation. As mentioned in introduction, we restrict scope of this research to purely foreign awards, that is, awards rendered by foreign arbitral tribunals located outside the Russian territory.

One cannot underestimate importance of guaranteeing finality of awards. It ensures certainty, predictability and efficiency in the international arbitration process that is necessary for international trade development. To guarantee effective arbitration, arbitration statute must
generally prohibit judicial interference in the arbitration and must permit prompt, unburdensome, and reliable enforcement of arbitration agreements.\textsuperscript{20}

It is important to clarify what we mean by recognition and enforcement of foreign arbitral awards. First, a party to an arbitration may seek recognition of an arbitral award.\textsuperscript{21} Recognition is the national court proceedings that amount to a judicial decision (exequatur).\textsuperscript{22} It acknowledges the existence of the arbitration and recognises the decision made by the arbitration tribunal.\textsuperscript{23} Most typically, a successful respondent will seek recognition of an award to preclude the disappointed claimant from relitigating its claims.\textsuperscript{24} In other words, recognition acts as a shield by preventing court proceedings from being held in respect of decided matters.\textsuperscript{25}

Enforcement either follows or is simultaneous to recognition and gives effect to the mandate of the arbitral award.\textsuperscript{26} Thus, enforcement is a sword which successful party uses to request the assistance of the court in enforcing the award.\textsuperscript{27} This involves commencing legal proceedings, under local law, where the award provides the basis for coercively appropriating money or imposing other consequences on the “award-debtor.”\textsuperscript{28} Court sanctions include seizure of the award debtor’s property, freezing of bank accounts or even custodial sentences as extreme measures.\textsuperscript{29}

The review of awards occurs both at the seat of the arbitration (where actions to set aside will take place) and in all countries where enforcement of the award is sought.\textsuperscript{30} Recognition and enforcement provide official recognition of the arbitration process and confirm its product.\textsuperscript{31} It makes these procedures vitally important in arbitration.

A short overview of the procedure has shown that international arbitration has mechanisms for enforcing arbitral awards all over the world to make the unsuccessful parties to pay their debts. However, these mechanisms are not panacea and obstacles to enforcement may arise. Namely, the NYC states that recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, if properly proved, in cases of:

\textsuperscript{20} Donovan p. 648  
\textsuperscript{21} Born 2001 p. 705  
\textsuperscript{22} Lew et al. p. 689  
\textsuperscript{23} Lew et al. p. 689  
\textsuperscript{24} Born 2001 p. 705  
\textsuperscript{25} Lew et al. pp. 689  
\textsuperscript{26} Lew et al. p. 691  
\textsuperscript{27} Lew et al. p. 690  
\textsuperscript{28} Born 2001 p. 705  
\textsuperscript{29} Lew et al. p. 691  
\textsuperscript{30} Lew et al. p. 689  
\textsuperscript{31} Lew et al. p. 688
– incapacity of a party to the agreement/invalidity of the agreement under applicable law (Article V 1 a);
– a party being not properly noticed of the appointment of an arbitrator or arbitration proceedings/a party being otherwise unable to present his case (Article V(1)(b);
– the award dealing with a difference not contemplated by or not falling within the terms of the submission to arbitration/the award containing decisions on matters beyond the scope of the submission to arbitration (taking into account separability of invalid provisions) (Article V(1)(c);
– the composition of the arbitral authority or the arbitral procedure being not in accordance with the agreement of the parties/the law of the country where the arbitration took place (in the absence of agreement) (Article V(1)(d); or
– the award not yet binding on the parties/set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made (Article V(1)(e).

Under the second part of Article 5 of the NYC, the competent authority in the country where recognition and enforcement is sought can refuse recognition and enforcement by finding

– non-arbitrability of the dispute (“the subject matter of the difference is not capable of settlement by arbitration under the law of that country”) (Article V 2 a); or
– breach of public policy (“the recognition or enforcement of the award would be contrary to the public policy of that country”).

We can see that public policy defense together with the non-arbitrability are the only defenses that the competent authorities can invoke on their own motion, regardless whether the parties raise them. This undoubtedly brings unpredictability to the arbitration. The scale of this obstacle depends on the theoretical understanding of public policy in a certain country and practical implementation of this understanding. In light of this, it is vitally important to analyse what international standards mean by public policy.

2.2. Definition of public policy

It is important to define public policy for following reasons. First, it allows to structure approach of further research and categorise directions of more detailed research. Secondly, it helps us to find the common point for different national jurisdictions. Thirdly, it allows us to identify factors that influence the changes in the interpretation of public policy.
Researchers have discovered a so-called public policy paradox. Namely, public policy exists in many legal systems but one often cannot define it correctly neither in theory nor in practice.\textsuperscript{32} Courts and commentators often treat public policy as a potential "loophole" in binding international arbitration.\textsuperscript{33} They refer to the ease with which a court might disregard a foreign arbitral award for virtually any reason simply by finding that enforcement of the award would contravene the public policy of the forum.\textsuperscript{34}

Definition of public policy consists of several elements. Compound parts of the definition include aims that it pursues, classification of public policy and its basic features. This chapter will provide an overview of these elements in general theory and the next chapter will focus on peculiarities of compound elements of public policy under Russian legal theory.

The public policy concept is complex and difficult to define because its aim is to determine several things: the meaning of the arbitration clause, the procedures of the arbitration and the content of the award itself.\textsuperscript{35} We believe that this multitude of roles is caused by the tendency to interpret public policy concept widely and the lack of coherent evaluation of general legal nature of public policy.

Notion of public policy differs among different national jurisdictions and its changes depend on changes in societal values.\textsuperscript{36} Various states perceive the degree of fundamentality of moral conviction or policy differently for every case.\textsuperscript{37} One can find some underlying commonalities. For instance, cases when the upholding of the award would “shock the conscience” or is “clearly injurious to the public good” often fall under public policy exception.\textsuperscript{38} Schlosser argues that the use of public policy defense is only justified “where the non-conformity with basic principles of morality and justice is evident”.\textsuperscript{39} Jurisdictions have different approaches to defining the level of required violation of public policy. The violation must be “clear”, “concrete”, “evident” or “patent”, “blatant”, “manifest”, “obvious and manifest”, “flagrant”, “particularly offensive”, “severe”, “intolerable”, “unbearable”, “repugnant to the legal order”, etc.\textsuperscript{40} However, we believe that the aforementioned standards contribute mostly to the vagueness of public policy concept and create an additional excuse for enforcement courts to refuse recognition and enforcement of foreign arbitral awards in other to “protect morality”.

\textsuperscript{32} Pavlova
\textsuperscript{33} Junker p.228
\textsuperscript{34} Junker p.228
\textsuperscript{35} De Enterria p.390
\textsuperscript{36} Wires p.5
\textsuperscript{37} Fry p. 90
\textsuperscript{38} Poon p. 188
\textsuperscript{39} Liebscher p. 82
\textsuperscript{40} IBA Report p.11
There exist various approaches to defining public policy across different legal systems. Civil law countries refer to public policy as the foundation of the legal system, on which society’s moral, political or economic order rests. Common law countries refer to more widely defined, abstract fundamental values.\(^{41}\) In the United States, the award breaching public policy must be contrary to the forum’s “most basic notions of morality and justice”. The English standard requires the award being “clearly injurious” or “wholly offensive”.\(^{42}\) In a minority of jurisdictions, public policy gets much broader interpretation.\(^{43}\) Moreover, it is important to highlight that public policy includes not only purely legal aspects. Evaluation of the damage to the sovereignty of the state and interests of big social groups mostly depends on political rather than legal values and concepts.\(^{44}\) Further research will show that courts in their reasoning regarding public policy often appeal to vague philosophical terms when trying to define the limits of public policy.

A clear definition would increase the simplicity and certainty of arbitration in the context of international trade and therefore promote the main goals of alternative dispute resolution.\(^{45}\) However, public policy does not have an extensive definition neither in the NYC nor in any other international instrument. Lack of normative regulation creates problems in defining public policy in practice.\(^{46}\) In its turn, it creates the need to research deeper the case law in this sphere.

Case law also forms essential recommendations for application of public policy. Researching foreign law on interpretation of substantive public policy does not fall under the scope of the thesis. However, it is important to highlight one important case that has established a universal standard on approaching substantive public policy. Namely, the Court of Appeal in *DST v Rakoil* highlighted that one cannot exhaustively define notions of public policy and therefore should approach them with extreme caution.\(^{47}\) This case has also established a general standard for public policy exception that is applicable for different jurisdictions. Under this standard, it has to be shown that “there is some element of illegality or that the enforcement of the award would be clearly injurious to the public good or, possibly, that enforcement would be wholly offensive to the ordinary reasonable and fully informed member of the public on whose behalf the powers of the state are exercised”.\(^{48}\) Further studies of mentality will help us to trace how different values and goals are balanced in practice.

\(^{41}\) IBA Report p.6  
\(^{42}\) Curtin p.277  
\(^{43}\) IBA Report p.6  
\(^{44}\) Kurzinsky-Singer p. 198  
\(^{45}\) Cole p. 382  
\(^{46}\) Fry p. 92  
\(^{47}\) Lew et al. p. 721  
\(^{48}\) Lew et al p. 721
The balance between interests of states and goals of internationalisation depends on the concrete public policy in question and its importance vis-a-vis the promotion of international arbitration as a competing policy.\(^\text{49}\) Further research of mentality will help us to trace how different values and goals are balanced in practice.

This discussion has shown us that public policy exception means a serious violation of fundamental rules of a certain society. Fundamental rules are defined based on societal values, political and legal concepts, which, in its turn, depend on multitude of factors. Vagueness of public policy concept has created the need to regulate it internationally. Therefore, before turning to mechanisms of how national law approaches public policy, it is important to research the international framework for public policy exception.

### 2.3. International regulatory framework of public policy

Public policy exception is stated in international conventions, bilateral treaties and is further referred to in national legislation. The NYC has the most global impact and thus we will start our analysis from it. Apart from that, regional conventions, bilateral treaties and model laws refer to public policy. We believe that it is important to tackle them as well, as even in cases when such international sources do not have a direct legal effect, they still affect development of theoretical legal thought and mentality regarding public policy.

The goal of the NYC was to provide uniform procedures for enforcing foreign arbitral awards and minimise discrepancies between different national jurisdictions.\(^\text{50}\) Increasing demand of international business for the advantages of arbitration has also remarkably influenced formation of the NYC.\(^\text{51}\) In summer 1958, a brief Mission Statement formulated the main goal of the NYC: “Worldwide simple enforcement of arbitral awards”.\(^\text{52}\) The NYC was called an “important step forward”, a considerable success and the beginning of a new “Esperanto” of international arbitration law.\(^\text{53}\) It has also started a trend toward delocalisation of arbitral law.\(^\text{54}\) In our view, this clear statement of goals and aspirations played one of the major roles in the building of substantial political weight of the NYC.

The NYC imposes a general obligation on contracting states to recognise and enforce awards. Under the NYC, a successful claimant can seek enforcement of the award either in the national

---

\(^{49}\) Poon p. 190  
\(^{50}\) ILA Report p. 5  
\(^{51}\) Cole p. 368  
\(^{52}\) Nariman p. 11  
\(^{53}\) Cole p. 382  
\(^{54}\) Gibson p. 103
court of the seat of arbitration or the court of the country in which the respondent has its assets.\textsuperscript{55} Article III of the NYC requires contracting states to recognise awards made in other countries and prohibits putting foreign arbitral awards under procedural requirements more onerous than those for domestic awards.\textsuperscript{56} Article V lists the exclusive grounds for refusing to recognise and enforce foreign arbitral awards (see 1.1.1). Public policy defense can be invoked either by the party or by the court (Art. V 2 b of the NYC). These provisions provide internationally uniform and transparent standards of proof and aim to prevent parochial resistance to the recognition of foreign awards in the guise of formal requirements of proof.\textsuperscript{57} However, further research will illustrate what stumbling blocks to complying with international standards arise in practice.

From our point of view, despite ongoing debate on this issue, there is a little doubt that Article V(2)(b) of the NYC refers to the public policy of the recognition forum, that is, the public policy of the country where the party files a claim on recognition and enforcement of a foreign arbitral award. This is explicit in the text of the clause, which refers to the public policy “of that country”, as well as in the basic structure of Article V(2) as an exceptional escape device.\textsuperscript{58} This wording allows enforcement states to define public policy and thus retain a measure of control over international arbitration.\textsuperscript{59}

Provisions on public policy exception have been implemented into model legislation and regional international treaties. Both articles 34(1)(b)(ii) and 36(1)(b)(ii) of the UNCITRAL Model Law on International Commercial Arbitration of 1985 include public policy as a ground for refusing recognition and enforcement of a foreign award.\textsuperscript{60} The UNCITRAL Model Law assists states in modernising their laws on arbitral procedure to keep up with modern needs of international commercial arbitration.\textsuperscript{61}

There are also certain regional conventions that have influenced the formation of the playing field. Namely, that are the 1961 European Convention, the 1965 Washington Convention, the 1972 Moscow Convention, the 1975 Inter-American Convention on International Commercial Arbitration (Panama Convention) and the 1987 Arab Convention on Commercial Arbitration. The 1961 European Convention deals with the enforcement of foreign awards indirectly by merely restricting the grounds to refuse enforcement of awards to those provided for in the NYC.

\begin{itemize}
\item \textsuperscript{55} Ozumba
\item \textsuperscript{56} Born 2015 p. 275
\item \textsuperscript{57} Born 2014 p.3395
\item \textsuperscript{58} Born 2015 pp. 375 - 416
\item \textsuperscript{59} Fry p. 93
\item \textsuperscript{60} Villiers p. 160
\end{itemize}
Pursuant to Articles 53 and 54 of the 1965 Washington Convention, each member state is under obligation to recognise an award rendered under the Washington Convention and enforce the pecuniary obligations imposed by the award, as if it were a final judgment of the court in that state. The 1972 Moscow Convention has lost its importance as most of its member states have either withdrawn their membership or ceased to exist. Even though formally the Russian Federation is still a party to the Moscow Convention, Khvalei highlights that it has become outdated because it has not been actually used by the parties. The 1975 Inter-American Convention on International Commercial Arbitration (Panama Convention) and the 1987 Arab Convention on Commercial Arbitration play enormous role in the respective regions. This shows that the NYC is the most universally applicable international convention with the widest coverage that has set standards for the regional conventions.

The International Law Association (ILA) issued Final report on public policy as a bar to enforcement of international arbitral awards in 2002 with the aim to give a more detailed definition to the concept of public policy (ILA Report). The ILA Report is split into specific recommendations (ILA Recommendations) on applying public policy followed by detailed reasoning for providing these recommendations. The ILA Report highlights the exceptional nature of the public policy defense while stressing the fundamentality requirement for public policy principles, catalogues the compound elements of the public policy concept and specifies the source of law to be applied when assessing a potential public policy violation. Professional community now increasingly regards ILA Recommendations as reflective of best international practice. This makes ILA Report important and handy comparative tool to track the compliance of the Russian courts with international enforcement trends. We will use ILA Report as a comparison tool to assess compliance of the Russian courts with international standards.

This discussion shows that public policy cannot exist in vacuum. Its features are concretised through application of the concept, that is, actual interpretation of the international conventions, namely, the NYC. Exploring the procedure of applying public policy will help us to define main stakeholders and practical issues that influence interpretation of the concept in question.

2.4. Applying public policy under the New York Convention

---

62 Lew et al. pp. 694-696
63 Lew et al. pp. 694-696
64 Lew et al. pp. 694-696
65 Khvalei 2012 pp. 6-8
66 Lew et al. pp. 694-696
67 Gibson p. 134
68 Gibson p. 107
The NYC applies both to foreign and “non-domestic” awards, Namely, Article I (1) of the NYC states that “[t]his Convention shall apply to the recognition and enforcement of arbitral awards made in the territory of a State other than the State where the recognition and enforcement of such awards are sought”. It then adds that “[i]t shall also apply to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought.” Under the NYC, the “non-domestic” arbitral award may cover three categories of awards:

(i) an award made in the enforcement State under the arbitration law of another State;

(ii) an award made in the enforcement State under the arbitration law of that State involving a foreign (or international) element;

(iii) an award that is regarded as “a-national” in that it is not governed by any arbitration law”.

In fact, national legislation generally prescribes different standards for the annulment and recognition of “foreign” awards and locally made awards. Our scope of research is restricted to the recognition and enforcement of purely foreign arbitral awards (awards rendered by foreign arbitral awards located outside Russia). However, in our research we will look into some decisive cases on the enforcement of domestic arbitral awards (awards rendered by arbitral tribunals located in Russia) that have influenced the playing field for foreign arbitral awards as well.

Smit states four factors that public policy exception assesses: “(1) the arbitration agreement may violate public policy; (2) the conduct of the arbitration may violate public policy; (3) the law the arbitrators apply may violate public policy; and (4) enforcement of the award may violate public policy.”

Ma defines three stages in applying public policy, namely:

(i) Defining whether the alleged public policy falls within the public policy exception;

(ii) Defining whether the enforcement of the award would be contrary to the public policy;

(iii) Defining whether the enforcement court should allow enforcement despite the establishment or applicability of the public policy exception.

The public policy exception sets aside only those awards that are not covered by more specific grounds for refusal of enforcement and therefore plays a role of a residual clause. Authors of

---

69 Van der Berg pp. 2-3  
70 Born 2015 pp. 375 – 416  
71 Smit  
72 Ma p.1  
73 De Enterria p. 403
the NYC intended that enforcement should be refused only in limited circumstances.\textsuperscript{74} Application requires a direct violation of public policy; the mere involvement of notions of public policy is not enough.\textsuperscript{75} An enforcement court shall find a proper balance between aims of finality and justice.\textsuperscript{76} Therefore, we can view the interpretation task of the enforcement courts as a task of balancing the interests of different stakeholders of the recognition and enforcement proceedings.

When applying public policy under the NYC the enforcement court cannot review the merits of an arbitral award. This principle is best reflected in decision by Feldman J in Canada who held that courts “should not, under the guise of public policy, reopen the merits of an arbitral award on legal issues...where there has been no procedural misconduct”.\textsuperscript{77}

Varying linguistic versions of the NYC pose a question of interpreting public policy. The French text of the Convention, which is considered equally authentic, uses the term \textit{ordre public}, which may have own specific meaning under national laws.\textsuperscript{78} “May” wording of the Article V of the NYC attracts even greater attention. It states that enforcement ‘may be refused’ only if one of the seven grounds is satisfied, not that it ‘must be refused’. The “may” clause has been interpreted as allowing the enforcement court to enforce the award even if one of the seven grounds for refusing enforcement is satisfied.\textsuperscript{79} The Russian, Spanish and Chinese texts are identical in meaning. In fact, only the French text supposedly establishes an obligation to deny recognition to awards that have been annulled in the arbitral seat. In fact, the better view is that the French text is ambiguous letting the English wording prevail.\textsuperscript{80} However, a court cannot disregard its own mandatory legal provisions regarding public policy, and must determine the right answer in this respect rather than allow it to depend exclusively on the quality of the arguments and evidence presented by a private party.\textsuperscript{81}

Furthermore, Article V(2) is governed by the doctrine of \textit{lex specialis} (the doctrine that a law governing a general subject matter does not override a law which governs specific matters). The Swiss Supreme Court stressed that the purpose of the public policy clause is to cover other matters not addressed in Article V(1). However, in many cases, the same situation is considered

\textsuperscript{74} ILA Report p2  
\textsuperscript{75} De Enterria p. 406  
\textsuperscript{76} ILA Report p. 2  
\textsuperscript{77} Wires p. 22  
\textsuperscript{78} Cole p.375  
\textsuperscript{79} Mcilwrath & Savage p. 354  
\textsuperscript{80} Born 2015 pp. 375 - 416  
\textsuperscript{81} Paulsson pp. 217 - 232
under both Article V(1) and (2) simultaneously. The Swiss approach is preferable in light of different evidentiary requirements and scope under Article V(1) and V(2).  

Based on this, we can highlight several limitations of the NYC. First, different wording of public policy inevitably results in differences in interpretation and implementation in different jurisdictions. Secondly, the wording of court obligations in approaching public policy exception differ across language versions of the NYC. Thirdly, the NYC is silent on how to approach an overlap of grounds under Articles V(1) and V(2) of the NYC. These issues further complicate practical understanding of public policy. One of the ways to minimise this vagueness is to try to comprehend how public policy balances various interests of involved stakeholders.

2.5. Role and impact of public policy

In addressing the role of public policy, it is important to discuss the impact of this concept on legal system in general, as well as to concretise its impact on different stakeholders (state courts, arbitral tribunals and international business). This will help us to better understand the behavior of parties that bring certain arguments in the court proceedings and reasoning of courts that have a wide discretion in interpreting public policy.

2.5.1. Impact on legal systems

Public policy exercises a negative function. Negative function of public policy deprives the foreign law of its normal title of application or the foreign act of its faculty to be recognised. It also constitutes a limit to the functioning of the rules of private international law when those rules regulate either the application of foreign law or the recognition of a foreign act.

The role of public policy is not only to protect the public interest but also to restore the justice. The injustice may stem from breaches of both procedural and substantive laws. Public policy provides for a flexible response to unforeseen consequences of forum recognition of foreign acquired rights. The overarching purpose of public policy to protect a legal system's core values justifies a unified treatment, despite existing variations resulting from the different legal environments. Completely automatic operation of conflicts rules produces mechanical and unjust results in cases where a court may be able to guarantee a more equitable outcome. Also, we believe that such mechanical approach of courts may also incentivise mala fide behavior of

---

82 Kronke et al. p. 367.
83 Lalive pp. 260-261
84 Lalive pp. 260-261
85 Kurzynsky-Singer p. 200
86 Murphy p. 613
87 Zeiler et al. p. 140
88 Murphy p. 613
parties abusing interpretation of public policy in their own favour. Thus, we should not underestimate the need to apply public policy flexibly taking into account interests of various stakeholders.

2.5.2. Stakeholder analysis

Public policy plays insurmountable role for different stakeholders. Those include states, international commercial courts, parties, third parties, investors. The ILA Recommendations aim to create an appropriate balance between the interests of the stakeholders — the parties to a specific arbitration, members of the arbitration community generally, and the interests of the State. Indeed, these are the key stakeholders in the development of international commercial arbitration. 89

2.5.3. Impact on courts

The interplay between arbitrators and enforcement judges creates a system of checks and balances. 90 Yet, the effectiveness of international arbitration relies on the coercive powers of national courts. These courts may be eager to review awards for consistency with their own notions of public policy at the recognition and enforcement stage using mechanisms provided by the NYC. 91 Due to the ultimate control of national courts over the recognition and enforcement of arbitral awards, public policy can limit the denationalisation of international arbitration. 92 Therefore, it is important to secure the balance between rights and interests of the arbitral tribunals and state courts.

Many factors can affect the decision to apply a public policy exception to the enforcement of an arbitral award and, therefore, the balance of interests of the involved parties. These factors include the instructions of the parties, the connection of the national public policies with the underlying contract, the willingness of the parties to carry out the arbitral decision voluntarily, the nature of the policy in question, the purpose of the policy, and the attitude of national courts towards enforcement of foreign arbitral awards. 93 This shows that the foreign investors should be prepared for a deep research of legal culture in order to be able to identify risks connected with recognition and enforcement of foreign arbitral awards.

The U.S. Supreme Court highlighted in Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.: “The utility of the [New York] Convention in promoting the process of international arbitration..."
commercial arbitration depends upon the willingness of national courts to let go of matters they
normally would think of as their own.”94 We believe that this statement is also applicable for the
national courts of other countries as they all function under the same regulatory framework of
the NYC.

In practice, the courts face a dilemma. If the award is confirmed, the parties are permitted to
circumvent important legislative and judicial policies through mechanisms of arbitration. If the
award is vacated or modified, the policy favoring promotion of arbitration is frustrated as
arbitration becomes less acceptable to the parties.95 The courts, therefore, should act as guardians
of the public interest and must properly consider all relevant legislative and judicial policies when
deciding whether to enforce arbitration awards.96

Although the imposition of “substantially more onerous” conditions on the enforcement of
foreign arbitral awards than those imposed for enforcing domestic awards is forbidden by the
NYC, the NYC does not preclude the state from having less onerous conditions for enforcement
of foreign awards.97 We believe that this creates the stimulus for further development of
arbitration environment and building trust between arbitral tribunals and national courts. If fact,
if arbitral tribunals get a central place in the international legal order, national courts will need to
“shake off the old judicial hostility to arbitration”, and their customary unwillingness to cede
jurisdiction of a claim arising under domestic law to a foreign tribunal.98 Thus, the NYC provides
flexibility for the stakeholders to change their attitude to international commercial arbitration.

2.5.4. Impact on parties

Public policy mediates between the interests of international business and interests of the state
with the closest connection to the contract.99 Moreover, the party autonomy must be balanced
against the legitimate right of a state to protect its own processes and interests.100

A counsel with creative approach can often construct public policy or non-arbitrability arguments
in order to delay enforcement efforts.101 However, public policy can still act as a “tool for external
constraint”, limiting the freedom of members of the international business community to
determine their commercial relationships and to structure dispute resolution as they wish.102

94 Born 2014 p. 3659
95 Judicial review p. 547
96 Judicial review p. 574
97 Bouzari p. 212
98 Lanier & Dolinar p. 34
99 Gibson p. 106
100 Villiers p.179
101 Born 2016 pp. 133 - 136
102 Gibson p. 105
Further research will show how public policy concept can help both to restrict mala fide behavior of parties and act as an additional ground for mala fide strategies.

2.5.5. Impact on arbitral tribunals

There is a growing discussion on the authority and obligation of arbitral tribunals to consider issues of public law within the arbitration procedure itself.\textsuperscript{103} Public policy indicates the development of the arbitration.\textsuperscript{104} We believe that flexible and arbitration-friendly approach to interpretation of public policy will incentivise parties to avoid mala fide behavior, and arbitral tribunals to filter such mala fide behavior in order to strengthen own reputation. In longer run, it will contribute to the growth of trust between arbitral tribunals and enforcement courts.

It is evident that interpretation of public policy shall guarantee a proper balance between interests of involved stakeholders, especially in the view of growing internationalisation of commerce that strengthens the need for increasing arbitration friendliness. These needs are also reflected in classifications of public policy.

2.6. Classifications of public policy

There exist different approaches to categorise public policy. We will focus on the classifications that have practical implications and are vital for determining the scope of our research. Positive/negative public policy classification looks at how scope of public policy is defined. Substantive/procedural public policy classification determines what norms are breached. Finally, national/international public policy classification measures internationality of norms and values falling under scope of public policy. These classifications will help us to explore the limits to excessive interpretations of public policy and trace the development of theory of public policy, as well as to highlight the main risks when the enforcement courts confuse different types of public policy.

Positive public policy means that the national jurisdiction defines the scope of mandatory rules that cannot be breached when applying foreign law or enforcing a foreign act.\textsuperscript{105} Negative concept rather focuses on defining a limited scope of features of a foreign law or an act that makes it impossible for the jurisdiction to enforce them without a breach of overarching values.\textsuperscript{106}

It is evident from the discussion that negative policy concept is more arbitration-friendly as it is based on overarching principles, not the strict reference to positive norms of law.

\textsuperscript{103} Gibson p. 104
\textsuperscript{104} Gibson p. 111
\textsuperscript{105} Dzuskayeva & Ivanova p. 99
\textsuperscript{106} Dzuskayeva & Ivanova p. 99
First, we will analyse substantive and procedural public policy. Substantive public policy exception signals breach of substantive laws whereas procedural public policy indicates violation of procedural requirements. Born mentions following elements of substantive public policy: mandatory criminal law, corruption and bribery, trade sanctions, export controls, currency controls and similar regulations, illegal contracts, bankruptcy, penalties and liquidated damages, interest, duress and wrongful force, res judicata, statutes of limitations, pacta sunt servanda, good faith and related doctrines, application of incorrect substantive law, principle of proportionality.\textsuperscript{107} ILA Report has also included antitrust and competition law; equality of creditors in insolvency situations and state immunity to the public policy list.\textsuperscript{108} An example of a substantive fundamental principle is the principle of good faith and prohibition of abuse of rights (especially in civil law countries).\textsuperscript{109} Other examples include \textit{inter alia} pacta sunt servanda\textsuperscript{110}, prohibition against uncompensated expropriation and prohibition against discrimination.\textsuperscript{111} Procedural public policy includes requirements of adequate notice, an opportunity to be heard, equality of treatment and an impartial tribunal.\textsuperscript{112} Procedural public policy is much more often invoked and applied than substantial public policy.\textsuperscript{113} However, each alleged breach of procedural public policy shall pass a fundamentality test. Procedural public policy defense is only justified in cases of egregious departures from fundamental national standards of procedural protection.\textsuperscript{114} However, procedural public policy is based on more universal due process principles that are easier to establish on the international level. It makes application of procedural public policy slightly easier to predict. Substantive public policy requires more specific knowledge of pitfalls of the national jurisdictions, namely fundamental principles specific to national jurisdiction. Therefore, researching specifics on public policy under national legislation is vitally important to be able to identify risks arising in the enforcement process.

Every arbitration of a mandatory national law implicates one of following categories of public policy: domestic, international, or transnational.\textsuperscript{115} Sometimes even more detailed classification is used, defining subcategories of domestic, international, transnational, regional and truly international public policy.\textsuperscript{116}

\begin{thebibliography}{116}
\bibitem{107} Born 2014 p. 3671
\bibitem{108} ILA Report pp. 16-17
\bibitem{109} ILA Report p.6
\bibitem{110} Latin for “agreements must be kept”.
\bibitem{111} ILA Report p.6
\bibitem{112} Born 2014 p. 3683
\bibitem{113} EU Study p. 13
\bibitem{114} De Enterria p. 414
\bibitem{115} Curtin p. 281
\bibitem{116} Fry p. 85
\end{thebibliography}
We will use the classification suggested by Kessedijan as the most simple, clear and practically applicable one. Kessedijan concretises what one can mean by three levels of public policy. First, comes domestic public policy with little or no influence in the process of international arbitration. Secondly, there comes international public policy that encompasses a body of rules governing international conflict of laws. The third level of public policy extends international public policy by reconciling differing legal systems in order to form generally accepted principles to govern international business transactions.\textsuperscript{117} Let us analyse this classification in more detail.

Domestic public policies have changed over the years, influenced by factors such as national developments in the political and legal system, the involvement of the national economy in international trade, and political decisions (e.g. promotion of foreign investment).\textsuperscript{118} In practice, courts adopting the narrow interpretation of public policy actually distinguish between the enforcing state's domestic public policy and its international public policy.

Internationalisation of arbitration creates the stimulus for development of international public policy concept. Although Article V(2)(b) refers to the “public policy of that country”, the contracting states are not completely free in their interpretation of the public policy concept.\textsuperscript{119} The application of international public policy means that public policy is rarely a ground for refusing enforcement of international arbitral awards.\textsuperscript{120} International public policy is characterised by a more limited content and a more narrow application than domestic policy.\textsuperscript{121} The Court noted in \textit{Mitsubishi Motors Corporations v Soler Chrysler-Plymouth Inc}. that it will be necessary for national courts to subordinate domestic notions of arbitrability to the international policy favoring commercial arbitration’.\textsuperscript{122} The equating of "national policy" with United States “public policy” was considered a mere “parochial device protective of national political interests [that] would seriously undermine the Convention's utility”.\textsuperscript{123} As this reasoning is based on the universally applicable principles of the NYC, it is relevant for analysing enforcement trends also in other jurisdictions. In light of this, in 2003 the International Law Association (ILA) endorsed the use of international public policy.\textsuperscript{124} ILA recommends that “[t]he finality of awards rendered in the context of international commercial arbitration should be respected save in exceptional circumstances”, meaning the violation of international public

\textsuperscript{117} Terez p.7
\textsuperscript{118} Böckstiegel p.2
\textsuperscript{119} Villiers. Pp. 166-167
\textsuperscript{120} ILA Report p. 4.
\textsuperscript{121} De Enterria p. 396
\textsuperscript{122} Villiers p.166
\textsuperscript{123} Junker p.240
\textsuperscript{124} Villiers p. 166
policy. Much that might violate domestic public policy is permitted in the context of international public policy in order to encourage international trade. When considering a foreign arbitral award, the enforcement courts interpret international public policy only as the most basic principles of morality and justice, while in relation to local judicial and arbitral judgments, they are ready to interpret public policy more broadly (that is, apply the concept of domestic public policy). However, still in some jurisdictions, the reference to public policy is clearly seen as a reference to domestic public policy. Thus, in such cases, enforcement courts exert a stricter control on alleged violations of public policy. Those tendencies illustrate how important it is to bear in mind “dualism” (domestic/international) of public policy in assessing its interpretation in practice.

ILA Report provides us with the list of situations that fall under the concept of international public policy in accordance with the NYC. Under Recommendation 1(d) of ILA Report, the international public policy of any state under Article V(2)(b) includes: “(i) fundamental principles, pertaining to justice or morality, that the state wishes to protect even when it is not directly concerned; (ii) rules designed to serve the essential political, social and economic interests of the state, these being known as *lois de police* or public policy rules; (iii) the duty of the state to respect its obligations towards other states or international organizations”. This notion of an international public policy has been described as “more restrictive”, “more narrow”, “more tolerant”, or “milder” than its purely domestic sibling. Doctrine of international public order includes basic standards of good faith and regulations of the widely adopted uniform rules and international codes of conduct. Popular examples of violations of international public policy include biased arbitrators, lack of reasons in the award, serious irregularities in the arbitration procedure, allegations of illegality, corruption or fraud, the award of punitive damages and the breach of competition law. It shows that international public policy is a narrowly defined concept that relies on universally acceptable principles.

Finally comes the vague concept of transnational public policy. An enforcement court should consider transnational public policy only when the arbitration is both international in nature and subject to the lex mercatoria. Thus, transnational public policy is a hybrid between

125 Blackaby et al. pp. 605 - 662  
126 Harris, pp. 10-11  
127 Tapola, p. 179  
128 IBA Report p. 5  
129 IBA Report p. 5  
130 Schwarz & Ortner p. 152  
131 Tapola p. 180  
132 Lew et al. p. 722  
133 Curtin p. 281
international public policy and the lex mercatoria.\textsuperscript{134} European public policy can be seen as a regionalised transnational public policy concept.\textsuperscript{135} However, more skeptic opinions also exist. Skeptics believe that the NYC anyway acknowledges the ultimate right of State courts to determine what constitutes public policy within their jurisdictions.\textsuperscript{136} In practice, courts will only invoke “transnational public policy” if they consider it a part of the international public policy of the state in question.\textsuperscript{137} According to them, no uniformity exists regarding public policy rules and there is nothing today to be called transnational public policy.\textsuperscript{138} International public policy practical application is heavily influenced by domestic policy, and transnational public policy is still just an ideal. As a result, there exist “as many shades of international public policy as there are national attitudes towards arbitration”.\textsuperscript{139} Court enforcement of awards without any encroachments of national legal particularities would be “a logical impossibility, like both having and eating the proverbial cake”.\textsuperscript{140} In other words, researchers agree that international public policy is more an idealistic concept than reality. In fact, even though public policy is sought to be international and globally oriented, its basis remains national and still the national judges in fact apply the public policy.\textsuperscript{141} Therefore, the public policy requires consideration of both domestic and international principles, while the NYC imposes international limits on national law public policies that are applicable in the recognition forum.\textsuperscript{142}

Public policy principles are not always objective or rational.\textsuperscript{143} They also shift easily based on the mood of the society or its leaders or rulers.\textsuperscript{144} However, self-interest has taught nations to relax, with respect to international transactions, many of the rules of domestic public policy, so as to prevent international business from channeling big transactions away to other more favourable jurisdictions.\textsuperscript{145} We believe that the balance between relaxation of enforcement procedures and prevention of abuse of rights by the parties to the dispute is still to be found. We will explore this balance further in our research.

\begin{flushleft}
\textsuperscript{134} Curtin p. 281
\textsuperscript{135} Schwarz & Ortner p. 159
\textsuperscript{136} Mayer & Sheppard p. 117
\textsuperscript{137} Hanotiau & Caprasse p. 731
\textsuperscript{138} Okekeifere p. 4
\textsuperscript{139} Lew et al. p. 719
\textsuperscript{140} Lew et al. p. 731
\textsuperscript{141} Tapola p. 178
\textsuperscript{142} Born 2014 p. 3651
\textsuperscript{143} Okekeifere p. 2
\textsuperscript{144} Okekeifere p. 2
\textsuperscript{145} Okekeifere p. 2
\end{flushleft}
To sum it up, national/international policy classification helps to evaluate the scope and scale of public policy in question. Clarifying these distinctions will also help us to distinguish between public policy and grounds that are close to public policy.

2.7. Public policy versus other grounds

Both in theory and in practice, public policy overlaps with other grounds for refusal to recognise and enforce foreign arbitral awards. It is important to study this overlapping. First, it helps to further analyse specific features of public policy and its complex structure. Secondly, it helps to clarify the scope of this research. Thirdly, it helps us to identify main obstacles the enforcement courts encounter in trying to understand what stands behind a vague term of public policy. In practice, public policy exception is most likely to overlap with cases where due process requirements are breached or the parties fail to comply with the regulations on the arbitrability of disputes.

First, we will look into how concept of public policy overlaps with the concept of due process. A possible overlap between substantive and procedure strongly affects the scope of a court’s review of the enforceability of awards. Substantive/procedural dichotomy is problematic, since violation of either substantive or procedural exceptions may deal with both procedural and substantive laws of the enforcement forums.\textsuperscript{146}

Under Article V(1)(b) of the NYC recognition and enforcement of the award may be refused if the party resisting enforcement furnishes proof that he was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case. Due process is also breached if under Article V(1)(d) the composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place.

It is subject to discussion whether procedural grounds which may be invoked to resist the enforcement of a foreign award under Article V(1)(b) and (d) of the Convention may also be raised as separate grounds under Article V(2)(b).\textsuperscript{147} Nevertheless, in fact, a violation of the fundamental principles of procedural law may fall within the public policy category.\textsuperscript{148} Actually, only serious procedural irregularities may lead to the non-enforcement based on the public policy

\textsuperscript{146} Junita p. 49
\textsuperscript{147} IBA Report p. 13
\textsuperscript{148} Junita p. 53
defense. Despite the overlap between the public policy and the due process exceptions, the enforcement courts should avoid treating them together, unless they are based on the same factual foundations. ILA also reminds the enforcement courts to consider the public policy exception on their own motion, especially when failure to do so may risk injustice. This allows the enforcement courts to exercise their control to prevent gross violations of due process on their own motion.

Interaction between concepts of the violation of public policy and non-arbitrability is also subject to discussion. Public policy concerns the very beginning and basis of the arbitration, namely formation of the arbitration agreement or arbitration clause. Thus, we can see that public policy is relevant for arbitrability. Public policy under Article V(2)(b) of the NYC is often seen as closely related to the non-arbitrability exception in Article V(2)(a) of the NYC. Some argue that non-arbitrability in essence forms part of the general concept of public policy and therefore article V(2)(a) is superfluous. Others argue that while arbitrability rules may be mandatory in character, they do not necessarily reflect fundamental national policies. Mandatory rules are not necessarily identical with public policy rules as public policy requires further additional qualifications. In other words, not all due process breaches are excessively serious and fundamental.

We believe that it is important to analyse interaction between public policy and non-arbitrability from a bit different perspective. The issue of arbitrability is an issue for the law of the enforcement state and, being governed mostly by public policy, varies from state to state. While a particular dispute would be non-arbitrable in a certain state on public policy grounds, it could be arbitrable in another on considerations of enlightened national self-interest (public policy). Therefore, theoretically it is often separated from public policy, as well as in this research.

149 Junita p. 55  
150 Ma p. 12  
151 Ma p. 12  
152 Böckstiegel p.1  
153 Junita p. 56  
154 Magnusson p. 683  
155 Villiers p. 163  
156 Villiers p. 163  
157 Böckstiegel p.3  
158 Blackaby et al. Chapter 11  
159 Okekeifere p.6
This discussion shows that it may be challenging to distinguish between public theory and related grounds for refusal to recognise and enforce foreign arbitral awards. Understanding the scale of violation required to fall under public policy exception helps us to separate these grounds and avoid mixing them.

2.8. Conclusions: roadmap to analyse national public policy

Discussion so far has shown important characteristics of public policy. However, there is no fixed definition of public policy neither in international law nor in national legislation. As a result, enforcement courts form meaning of public policy in practice by giving more concrete interpretation in court rulings that, in its turn, affect future court rulings and legal thinking even in civil law countries. Research shows that in order to analyse national approach to public policy, we should address following issues:

- Historical development of public policy concept;
- main spheres and sources of legislation influencing the concept;
- mentality and legal culture of main stakeholders – courts of the enforcement jurisdiction, arbitrators, parties;
- role of the enforcement courts in interpretation of public policy and procedures of applying public policy exception.

We will use this scheme in researching public policy exception under Russian legal theory and regulatory framework in the next chapter, and we will refer to these factors when performing case law analysis in the last chapter of the thesis.

3. PUBLIC POLICY IN RUSSIA

3.1. Introduction

The roadmap for approaching national substantive public policy will help us to research the theoretical and practical interpretation of this concept in today's Russia and trace its development trends. This chapter will start with analysing historical aspects of development of the Russian public policy concept starting from the Soviet period. Based on this, we will be able to analyse the mentality and existing attitudes towards public policy. The theoretical framework that we have presented in the previous chapter will help us to look into the analysis of existing regulatory framework for substantive public policy concept in Russia. Specific attention will be paid to the role of case law in interpreting substantive public policy.
3.2. Emergence of public policy in Russian legal theory

Development of law and improvement of legislative techniques make it possible to identify the elements of public policy and fix them legislatively right on time and according to the needs of current public interests.\(^{160}\) Thus, at any time, interpretation of public policy has been a reflection of prevailing needs and values of the society.

The average soviet lawyer believed that the law was a product of the state and that no law could subsist without the state. A soviet way of thinking equaled internationalisation of the law to the degeneration of the law and the state.\(^{161}\) Soviet law had imperative character leaving private parties with almost no discretion in planning and establishing their commercial relations. Whereas in theory negative public policy concept prevailed, in practice, the concept of positive public policy was dominating.\(^{162}\) There were two concepts in soviet theory of private international law. Pereterskiy believed that the courts should assess the content of the foreign law itself.\(^{163}\) Luntz, in contrast, believed that not the foreign law, but the results of its application shall be subject to assessment for possible breaches of public policy.\(^{164}\)

Up until the middle of the nineties the court of the general jurisdiction were in search of right understanding of public policy category. That research often resulted in the review on the merits. Only in the end of the nineties, the Supreme Court of the Russian Federation succeeded to finally comply with the international standards, at least regarding enforcement of awards of international tribunals located in Russia (\textit{Omegatech Electronics GmbH vs state factory Izmeritel}, \textit{NANAoffshore vs ZAO Trast-Oil}).\(^{165}\) These positive trends were connected with slow changes in mentality, resulting in implementing more progressive legislation.

Now, public policy is usually translated into Russian as “the fundamentals of public law and order” or “the fundamental principles of Russian legislation”. The latter is the approach of the 1988 USSR Supreme Soviet Decree “On Recognition and Enforcement in the USSR of the Judgments of Foreign Courts and Arbitrations”, which formally still remains in force inasmuch as it does not contradict later legislation. Russian legislation uses almost the same approach in defining public policy.\(^{166}\) It shows that the theoretical definition of the public policy is not subject to notable changes.

\(^{160}\) D. Tapola pp. 248-249
\(^{161}\) Antonov p. 322
\(^{162}\) Muranov p. 5
\(^{163}\) Lopatin p. 89
\(^{164}\) Lopatin p. 89
\(^{165}\) Asoskov pp. 27-28
\(^{166}\) Antonov p. 329
The Ruling of the Supreme Court dated 25 September 1998 was actually a first attempt to define the content of the Russian public policy in the newest Russian history. The definition given by the Ruling equaled public policy with the “basics of the social formation of the Russian State”, almost repeating the definition formed in English law back in the 19th century. Namely, the House of Lords back in 1853 stated that public policy means the principle that forbids to do anything that would breach the fundamentals of any society. According to Tapola, the basics of social order beside legal norms also include basics of morals and ethics (customary norms) accepted in the society.

Before recognition and enforcement of foreign arbitral awards moved to the competence of the commercial courts, courts of general jurisdiction did not form detailed definitions of public policy. However, in the Ruling from 02 June 1999 the Supreme Court (the SCC did not exist at that time) indicated that by public policy one should understand general principles as stipulated by the Constitution and the laws of the Russian Federation. In 2000, the Supreme Court further noted that public policy means fundamentals of the legal order of the Russian Federation, which is bolstered first of all by the Constitution of the Russian Federation and the laws of the Russian Federation. Practitioners offer following definition: “public policy is a complex of aequi et bonae principles of the current legislation that compose the concept of the whole legal system of the concrete state and spheres of this system”.

Russian legal theory also provides its own classification of public policy. Neshatayeva distinguishes between narrow and broad interpretations of public policy. The narrow public policy is restricted to the general principles of the Russian law. The broad public policy also includes basic moral principles, main religious postulates, fundamental economic and cultural traditions, which are not directly stated in the legislation.

This discussion shows that public policy exception is applied taking into account historic peculiarities, specifics of legal system, level of scientific research and consistency of case law in

---

167 Tapola p. 193  
168 Baker et al. p. 7  
169 Traspo  
170 Tapola p. 194  
171 Bogatina  
172 Kazachenok p. 100  
173 Kazachenok p. 100  
174 Neshatayeva p. 560  
175 Neshatayeva p. 560
the given state. Krokhalev enhances the public policy exception with time and dynamic characteristics.

Dmitrieva believes that public policy includes four interrelated elements:

1. Basic fundamental principles of Russian law, primarily, constitutional, private law and civil procedure law principles;
2. Generally accepted principles of morality;
3. Legitimate interests of Russian citizens and legal entities of the Russian state and society;
4. Commonly recognised principles and norms of international law, which are part of the Russian legal system, including the international legal standards of human rights.

A short overview of theoretical approaches to defining public policy has shown that interpretation of public policy in Russia is not limited to purely legal aspects. In contrast, it heavily depends on historical and political factors as well as on prevailing mentality. We will address these compound elements of Russian public policy further in our research.

3.3. Mentality of stakeholders in enforcement of foreign arbitral awards

Russian practitioners compare public policy with a sophisticated surgical instrument created for the person with well-developed legal conscience. As René David highlighted, it is the “psychology of those to whom the law applies and those who are charged with its application” that really matters in comparative law. Therefore, it is vital to comprehend not only particular case law but, also, the legal mentality that underlies these decisions and the trend toward transforming this mentality in today's Russia. Thus analysis will help us to ensure the complex approach to the concept of public policy in Russian law and culture.

3.3.1. Mentality of the enforcement courts

In theory, the courts play an important control function, aiming at protecting the normal functioning of the social relationships when parties to them turn to dispute resolution mechanisms. In practice, however, Russian courts have shown an ambivalent attitude in relation to foreign dispute resolution. This is not surprising as Russia only in the last few decades

---

176 Minina p. 322
177 Tapola p. 175
178 Dmitrieva et al. p. 184
179 Davydenko & Khizunova
180 Antonov p. 321
181 Antonov p. 339
182 Kurochkin 2008
has opened itself up to private enterprise and international commerce.\(^\text{183}\) As a result, some Russian courts expansively interpret public policy, reallocate the burden of proof in favor of the party resisting enforcement, and sometimes examine the merits of the dispute.\(^\text{184}\)

In Russia, it was also common that lower instance courts refused to recognise foreign awards, and the SCC overruled these decisions, ordering enforcement.\(^\text{185}\) A Russian expert commented back in 1999 that many Russian courts still did not understand that their power is limited by the NYC, and that they were not entitled to review an arbitral award on its merits.\(^\text{186}\) Further research will show that this attitude may still be prevalent especially among courts of first instance.

Commercial courts have gained exclusive jurisdiction over enforcing foreign arbitral awards with the introduction of the new Russian Commercial Procedure Code (the CPC) in 2002. Before that, only courts of general jurisdiction dealt with these matters. As right after this reform the commercial courts were not prepared to deal with public policy, the parties managed to escape the liability by raising public policy defense. It obviously resulted in growing popularity of the public policy exception.\(^\text{187}\)

Professional community approached this court reform with caution also for other reasons. On the one hand, the judges of the commercial courts have much more experience in commercial matters.\(^\text{188}\) On the other hand, some senior judges take a hostile view of foreign arbitrators, whom they perceive as "anti-Russian".\(^\text{189}\) Others see public policy exception as a defensive filter preventing the application of foreign law.\(^\text{190}\) They also believe that arbitration represents a threat to their own jurisdiction by western companies with strong bargaining power.\(^\text{191}\)

We see public policy also as a political concept. It does not come as a surprise that much of the criticism has focused on the judiciary’s perceived lack of independence from political powers in Russia.\(^\text{192}\) However, in fact, reluctance of some judges to enforce the awards stems more from their incompetence in such matters and their suspicion against any non-state tribunals rather than on xenophobia.\(^\text{193}\) Especially courts of the first instance located outside Moscow and Saint Petersburg were reluctant to enforce foreign arbitral awards. The reasons for such reluctance were  

\(^{183}\) Antonov p. 338
\(^{184}\) Spiegelberger p. 352
\(^{185}\) Grishchenkova p. 440
\(^{186}\) Maurer p. 221
\(^{187}\) Zhiltsov
\(^{188}\) Nikiforov p. 788
\(^{189}\) Pellew
\(^{190}\) Traspov
\(^{191}\) Pellew
\(^{192}\) Baker et al. p. 2
\(^{193}\) Kulkov p.5
their skepticism of international arbitration, their inexperience, the excessive formalism of Russian law, and the courts’ inconsistent interpretation and application of the public policy exception.\textsuperscript{194}

In any case, state commercial courts have started to develop their own approach to public policy, which is prone to differ from approach of the courts of general jurisdiction.\textsuperscript{195} Somehow, this approach was affected by the abolition of the SCC in 2014. We will address these issues further in our research.

### 3.3.2. Mentality of the parties to the dispute

Debtors tend to use any slight difference between Russian legislation and foreign legislation to exploit the concept of public policy violation in their own interest. In other words, Russian defendants use public policy defense as a last resort in cases where none of the other grounds under Article V of the NYC are applicable.\textsuperscript{196} Unfortunately, Russian courts usually found in favor of debtors therefore awards were not enforced.\textsuperscript{197} It shows that, for the Russian business, the public policy has become a sort of universal magic wand used to negate any decisions of arbitral tribunals that are not favourable for them.\textsuperscript{198}

Perception of public policy among the parties to the dispute is combined with the paternalism of the state courts. Paternalism is partly justified by the modest experience of most Russian entities in international trade. At the same time, economic activities need the level of responsibility that cannot fully develop under the paternalist regime.\textsuperscript{199} Thus, finding a proper balance between interests of courts and private business is still ahead.

The research on public policy rarely addresses the mentality of the arbitral tribunals. However, it seems that growing attention to comparative legal research in the sphere of public policy can lead to growing awareness of arbitrators regarding trends in national laws.\textsuperscript{200} We believe that setting clear standards for public policy exception can strengthen compliance with international standards in arbitral tribunals in the longer run that has already been set by mechanisms such as IBA Guidelines on conflict of interests in international arbitration. In general, this analysis shows that practical implementation of public policy depends on the attitudes prevailing among the enforcement courts and parties that actively try to exploit the public policy exception. This

\textsuperscript{194} Kozmenko & Boog
\textsuperscript{195} Muranov p. 10
\textsuperscript{196} Hennecke & Machulskaya p. 4
\textsuperscript{197} Grishchenkova p. 448
\textsuperscript{198} Karabelnikov 2005
\textsuperscript{199} Kurzinsky-Singer p. 210
\textsuperscript{200} See, for instance, ICCA International Handbook on Commercial Arbitration Compare Jurisdictions at www.kluwerarbitration.com as an example of practical research tool.
understanding will help us to critically research existing sources of law that define (or may define) public policy in Russia.

3.4. Current framework of public policy in Russia

3.4.1 Legislation

Russian statutory law does not provide any clear-cut definition of public policy. This leads to an extensive interpretation of the concept. Some courts even equal public policy with the Russian legislation and refuse to enforce foreign awards that contravene certain provisions of Russian legislation. However, the unwillingness of the legislator to give the full definition of public policy is understandable. There are pragmatic reasons for that, as the content of public policy is in the constant process of development.

In any case, Russian law contains some orienteers for defining public policy. We can find hints on public policy from following sources:

- Constitution of the Russian Federation;
- substantive civil law (the Civil Code of the Russian Federation and laws adopted to concretise provisions of Russian Civil Code);
- procedural law (the Commercial Procedural Code of the Russian Federation (the CPC), the Civil Procedural Code of the Russian Federation), and

Russian law does not distinguish between international public policy and public policy of the Russian Federation and refer only to the latter in their decisions. In light of this, it is vitally important to research what Russian laws mean by public policy and how they define its role in recognition and enforcement of foreign arbitral awards.

Majority of Russian legal experts perceive contradiction to the public policy of the Russian Federation as a contradiction to the basics of legal formation of Russia as established by the

---

201 Ponty p. 450
202 Ponty p. 450
203 Karabelnikov 2005
204 Federal law on the arbitral tribunals in the Russian Federation regulated arbitration that had not been completed by the moment when Federal law on the arbitration in the Russian Federation entered into force.
205 Baker & McKenzie 2011-2012 p. 393
Russian constitution. Under Article 15(4) of the Constitution of the Russian Federation, treaties to which the Russian Federation is a party form a constituent part of the Russian legal system. Namely, the USSR signed the NYC back on 29 December 1958 and ratified it on 24 August 1960. This makes the NYC part of the Russian legal system. Under the terms of Article V of the NYC, Russia is obliged to recognise and enforce foreign arbitral awards unless one or more grounds apply under Article V.

On 27 July 2002, the Federal law on the arbitral tribunals in the Russian Federation was enacted to regulate arbitral tribunals established in Russia. Law of the Russian Federation No. 5338-1 dated 7 July 1993 “On international commercial arbitration” regulates international commercial arbitration and also establishes provisions on arbitration located outside Russia regarding interim measures and recognition and enforcement of foreign arbitral awards. The 1993 law on the international commercial arbitration (namely, Articles 35, 36 that regulate recognition and enforcement of foreign arbitral awards), as well as the NYC and Article 244 of the CPC use the term “public policy”. Articles 233 and 239 of the CPC use the expression “fundamental principles of Russian Law.” For the main Russian doctrine, those terms would define the same concept. Russian legislation on commercial arbitration was recently amended by two laws dated 29 December 2015. The first of laws, Federal law No. 382-FZ “On arbitration in the Russian Federation” is replacing the Federal law No. 102-FZ “On arbitration courts in the Russian Federation” regarding arbitration proceedings that were commenced on the Russian territory after 1 September 2016. It regulates commercial arbitration located in Russia. The second law, Federal law No. 409-FZ amends the number of other laws, including provisions of the Law of the Russian Federation No. 5338-1 dated 7 July 1993 “On international commercial arbitration” and provisions of the CPC on recognition and enforcement of foreign arbitral awards. Both laws entered into force on 1 September 2016. We will analyse most relevant amendments that this law has introduced further in our research.

The wording of the grounds to refuse to recognise and enforce foreign acts differ slightly under the Civil Procedural Code and in the CPC. The Civil Procedural Code lists as grounds for the refusal to recognise and enforce the judgment of a foreign court “the possibility of adversely affecting the sovereignty of the Russian Federation, jeopardising the security of the Russian Federation, or contravening the public order of the Russian Federation, whereas the Commercial

---

206 Tapola p. 188
207 Spiegelberger p. 354
208 Contracting States <http://www.newyorkconvention.org/countries> accessed 5 March 2017
209 Pellew
210 Zhiltsov
211 Ponty p. 450
Procedural Code only cites as grounds, instances where the judgment contravenes the public order of the Russian Federation”.\textsuperscript{212} This illustrates a more favorable regime for international commerce in comparison with non-commercial civil matters (e.g. family disputes, employment disputes), at least in theory.

Neither Articles 34-36 of the Law on international commercial arbitration, nor Article 244 of the Commercial Procedure Code provide definition of the public policy.\textsuperscript{213} There is a short reference to public policy in Article 1193 of the Russian Civil Code. Namely, it stipulates that “[r]efusal to apply norms of foreign law cannot be based solely on differences between the legal, political, or economical systems of the corresponding foreign state and the legal, political, or economical systems of the Russian Federation.\textsuperscript{214} In other words, the Russian legislation defines public policy in negative terms by stating what does not fall under public policy.\textsuperscript{215}

3.4.2 Role of the Supreme Commercial Court (2002-2014) in forming concept of substantive public policy

Russia is a civil law country meaning that in theory no court decision creates a binding precedent in the strict common law sense. However, decisions of higher courts can be very persuasive for the respective lower courts. Article 127 of the Constitution of the Russian Federation gave the SCC the power to issue guidelines of interpretation which are binding on the lower courts (before its abolishment in 2014). In fact, the decisions of the Supreme Commercial Court (the SCC) are virtually controlling and effectively reach value of statutory law.\textsuperscript{216} In addition, the SCC Presidium issued ‘informational letters’ (before the SCC was abolished) that are also not officially binding, but still highly persuasive. The role of information letters was to provide an overview of the certain topic with short conclusions providing guidance to approach the similar cases. The SCC Plenum rulings on specific issues are officially binding for all commercial courts.\textsuperscript{217}

The SCC Informational Letter No. 96 approving “Overview of commercial court practice on recognition and enforcement of foreign court decisions, on challenging the arbitral awards and issue of execution writ to enforce arbitral awards” dated 22 December 2005 (the 2005 Information Letter) summarised thirty-one cases decided by commercial courts of different levels, including the SCC, and provides recommendations to lower courts on deciding future

\begin{itemize}
\item[212] Moedritzer & Whittaker p. 108
\item[213] Karabelnikov 2008
\item[214] Antonov p. 333
\item[215] Zhukova & Pirogova p. 6
\item[216] Budylin p. 145
\item[217] Budylin p. 145
\end{itemize}
cases. In 2005 Information Letter, the SCC formulated the most detailed definition of Russian Federation public policy: “The international arbitral award can be deemed to violate Russian Federation public policy if its enforcement would result in actions expressly forbidden by law or causing damage to the sovereignty or security of the state, affecting interests of large social groups, being incompatible with the fundamental principles of various states’ economic, political and legal systems, disturbing citizens’ rights and liberties, as well as being contrary to basic principles of civil legislation, such as equality of the participants, inviolability of property and freedom of contract”. This shows that the SCC, even though not extending public policy to the whole Russian legislation, was rather in favor of broad interpretation of public policy. By this definition, the SCC effectively authorised the lower courts to review arbitral awards on its merits.

In 2013, the SCC Presidium issued Information Letter No. 156 dated 26 February 2013 “The review of the commercial court practice on cases of applying public policy when deciding to refuse recognition and enforcement of foreign court court rulings and foreign arbitral awards” (the 2013 Information letter). It provides an overview of case law that deals with public policy as a ground to deny recognition and enforcement of a foreign arbitral award. The SCC Presidium listed and commented on scenarios that may or may not constitute a violation of public policy as well as covered some general matters on applying public policy exception to enforcement. It has a vague approach to defining public policy. Namely, the 2013 Letter states that public policy is based on “fundamental legal principles characterised by supreme imperativity, universality, special social and public importance”. In this definition, the SCC refrains from the direct listing of principles and consequences that violate substantive public policy and instead adopts a more flexible approach, when consequences of recognition and enforcement of foreign arbitral awards should be analysed from the perspective of its influence on “fundamental principles”. Further research in the next chapter will show what consequences such a wide interpretation of public policy may incur.

Information letters show positive arbitration-friendly trends of enforcing foreign arbitral awards. Their adoption shows that the SCC has tried to reduce the use of “public policy” where this result is unjust. Whether or not Russian state courts will follow these guidelines remains to be seen.

---

218 Kozmenko & Boog p. 3
219 Davydenko & Kurzynsky-Singer p. 210
220 Ponty p. 451
221 Budylin p. 153
222 Kozmenko & Boog pp. 3-4
particularly in light of the abolishment of the SCC.\textsuperscript{223,224} In fact, the recent reform of the Russian court system calls into question whether the progress accomplished by the SCC will have any lasting effect on the enforcement practice of the Russian courts.\textsuperscript{225} Research of current Russian legislation and Information letters of the SCC shows that despite attempts to regulate public policy interpretation, consequences of its practical application are still unpredictable. We will further address the general notion of substantive public policy and the enforcement trends in the next chapter.

"The fact of the loss of the right to view the dispute in the arbitral tribunal and dealing with dispute in the state court cannot be viewed as a gross breach of rights of claimant"

(№ 305-ЭС16-19798, the order on the dismissal of the claim, Justice Pavlova)

4. SUBSTANTIVE PUBLIC POLICY IN PRACTICE

4.1 Introduction

Numerous authors address specifically substantive public policy in their research. However, their research does not address why exactly analysis of substantive public policy shall be prioritised inter alia before addressing procedural public policy. Researching substantive public policy is of prior importance for several reasons. First, it depends more on the knowledge of national laws and cultures in comparison with procedural policy. Secondly, parties believe that they will have less burden of proof when claiming breach of public policy than when claiming bias of arbitrators or absence of notification of the parties. Thirdly, substantive public policy more than procedural public policy depends on political mood and cultural peculiarities. Thus, it is important to both analyse the general award enforcement scheme and outline risks of misinterpretation of public policy arising at different court instances.

Research of Russian case law is complicated for several reasons. First, substantive legislation that comprises a basis for interpretation of substantive public policy is undergoing significant changes at the moment. Secondly, the system of Russian commercial courts that rule on recognition and enforcement of foreign arbitral awards has been reformed in 2014 as a result of abolishment of the SCC. In addition, there have been changes to regulation of court review proceedings in appellation and cassation instances. In light of this, the majority of research on interpretation of Russian substantive public policy in enforcement proceedings, especially

\textsuperscript{223} Grishchenkova p. 449
\textsuperscript{224} In June 2013, Russian President Vladimir Putin unexpectedly announced the creation of a new ‘super’ Russian Supreme Court that that would merge the Supreme Commercial (Arbitrazh) Court and the Supreme Court but actually meant the abolishment of the Supreme Commercial Court. See http://arbitrations.ru/press-centr/news/reformed-russian-supreme-court/
\textsuperscript{225} Hennecke & Machulskaya p. 15
research conducted in English is already out of date. Lastly, the information databases containing the court rulings in this field (kad.arbitr.ru, ras.arbitr.ru) are available only in Russian, and it is also problematic to access them from abroad for technical reasons. All these factors highlight actuality of the research aimed at defining practical interpretation of substantive public policy.

Researching substantive public policy includes following steps:

1. Analysing enforcement procedure will help us to comprehend risks of multiple reassessment of public policy exception in individual cases;
2. Determining stages of development of contractual relationship that are especially vulnerable to risks that parties or the court itself will find the circumstances that violate Russian public policy;
3. Structuring case descriptions in accordance with sequence of these stages.

This chapter will start with the overview of procedure of recognition and enforcement of foreign arbitral awards. Then, it will look at the role of fundamental principles of Russian law on the formation of public policy concept. Before proceeding to the analysis of cases, we will analyse approach we undertake in case analysis. Analysing most illustrative cases of the Russian law will help us to systematise main risks that foreign investors face during the enforcement proceedings in the Russian Federation.

4.2 Procedure of recognition and enforcement of foreign arbitral awards under Russian law

To understand the complexity of the matter, it is important to understand how many instances can actually be involved in forming and interpreting the concept of substantive public policy, and what pitfalls may be present at different stages of enforcement.

Foreign arbitral awards that do not require enforcement are automatically recognised in the Russian Federation without the need for any additional proceedings, if the interested party does not dispute it in one month after it got to know about this award. This rule was introduced by adding the Article 245.1 to the Commercial Procedure Code of the Russian Federation (the CPC). Amendments were introduced by Federal law from 29.12.2015 N 409-FZ in the framework on the reform of regulation of arbitral institutions in the Russian Federation.

However, in practice, it is quite likely that the debtor would not like to comply with the award voluntarily and would try to do its best to dispute it in the known legal environment. Both bona fide and mala fide parties may activate their knowledge of public policy exception to make courts apply it. In light of this, it is important to beware of a couple of things.
First, it is important to understand who is in fact most active in raising public policy defense. The NYC allows the courts to invoke public policy defense on their own motion. At the same time, if a party invokes arguments of public policy, a domestic court must nevertheless consider them. Secondly, it is important to understand what courts get the task to interpret the public policy and how they actually interpret it. According to the CPC, commercial courts ‘have the sole authority to decide whether foreign arbitral awards will be enforced.’

The scheme below illustrates that there is a complex system of commercial courts in Russia. The interested party may succeed in going through all the court instances up to the Supreme Court (before 2014 – up to the SCC) in the attempts to get recognition and enforcement of a foreign arbitral award/refusal to recognise and enforce. We refer to the court of the respective instance of the case review entitled to render a ruling on recognition and enforcement of a foreign arbitral awards as the enforcement court in our research.

Application for recognition and enforcement of a foreign arbitral award is filed with a commercial court at the place of the debtor’s domicile or, if it is not known, at the place where

Scheme 1. Instances of Russian commercial courts

---

226 Raschevsky et al.
227 Glusker p.606
the debtor’s assets are located. After considering the application for the recognition and enforcement of a foreign arbitration award, the commercial court issues a ruling (Article 245 of the CPC). The Commercial Apellation Courts examine the cases on the appeal and examine whether the courts of the first instance have rendered ruling lawfully and reasonably. The next instance is the Commercial Courts of the districts (Cassation Commercial Courts) that acts as the cassation courts for the rulings of the Courts of the respective court district. The cassation courts check whether the courts of lower instances have correctly applied norms of substantive and procedural laws. The Supreme Commercial Court as the court of last instance deals with cases in the framework of nadzor (overview) proceedings in case if courts of lower instances have grossly violated laws in examining the case. However, further case studies will show that quite many cases end up in the court of last instances when the lower courts fail to take all important circumstances into account when examining the case.

After giving the ruling on award recognition and enforcement, the court issues a writ of execution. If the debtor does not voluntarily execute the judgment, the claiming party initiates an execution procedure, which is similar to execution of domestic judgments of Russian state courts and is carried out by bailiffs. The bailiffs search for, attach and sell the debtor’s assets.

Russian courts remain very formalistic. Therefore, it is very important to follow scrupulously formalities of procedures, such as filing documents and translations in accordance with the formal requirements. Moreover, despite arrival of important guidelines by the SCC to lower courts on the application of the public policy exception in 2013, this concept remains very broad and vague. As a result, its application by the lower courts is often unpredictable. As it has been shown in the previous chapter, it depends on the level of legal culture and competence of the certain judge that is responsible for drafting the ruling. Understanding mentality may be a challenge for a foreign investor making the enforcement proceedings even more unpredictable in the eyes of involved foreign companies.

The enforcement courts are not allowed to review the merits of the case. In other words, if the party being against the enforcement of a foreign arbitral awards refers to the mistake in the application of material law, the enforcement court shall not review these arguments. It is well established in Russian case law. Back in 2006, the SCC Presidium clarified that the enforcement

---

228 Kulkov
229 Kulkov
230 Kozmenko & Boog p. 11
231 Kozmenko & Boog p. 11
232 Kozmenko & Boog p. 11
233 Getman – Pavlova p. 159
court does not reevaluate the factual circumstances established by the arbitral tribunal. In the case in question, the cassation court has not taken into account that it is the obligation of the arbitral tribunals to establish facts of the case. The arbitral tribunal has fulfilled its obligations and has examined that the loan was provided, and parties did not dispute this fact.\textsuperscript{234} In this ruling, the SCC highlighted that the cassation court cannot dispute the facts of merits established by an arbitral tribunal. Thus, the SCC complied with the general trends of the prohibition to review the case on merits, as evident, for instance, from the ILA Report. Namely, Recommendation 3(c) of the ILA Report states that “the court should undertake a reassessment of the facts only when there is a strong prima facie argument of violation of international public policy”. However, what would amount to “strong prima facie argument” is still subject to the discussion, so we would not address it further in our analysis.

Earlier, making the rulings of the court and their detailed reasoning public and open to everyone was a challenge. It was mostly stemming not from technological obstacles, but from the political will. For instance, in April 2001, the SCC Presidium overturned, on its own motion, several first instance decisions granting enforcement of an English award against a Russian debtor. The decree of the Presidium was not published. The Russian debtor appealed, but the Supreme Court refused application of appeal. The claimant published a long open letter to the Presidium in the newspaper, accusing the court of corruption. Despite seriousness of allegations, the President of the Court did not respond.\textsuperscript{235} Now digitalisation of courts is in significant progress. Kad.arbitr.ru and ras.arbitr.ru allows its users to trace the court proceedings and read the texts of interim and final court rulings in full for free.\textsuperscript{236} Also, services such as rospravosudie.com and commercial legal databases (ConsultantPlus, Kodeks, Garant) provide texts of the court rulings.

Moreover, it is important to evaluate only whether the result of recognition and enforcement of a foreign arbitral award (not an award itself) contravenes public policy.\textsuperscript{237} It does not matter whether the applied norms of the foreign substantive law correspond to the Russian legislation, the main concern is how a result of enforcement of such award would affect public policy.\textsuperscript{238} Only if the threat to public policy is real, and the state order cannot be protected by other means.

\textsuperscript{234} Ruling of the SCC Presidium dated 22 September 2006 (case No. 4438/06)
\textsuperscript{235} Pellew
\textsuperscript{236} However, for some reasons, access to these servers is restricted from outside the Russian Federation as of 26 February 2017.
\textsuperscript{237} Karabelnikov 2008
\textsuperscript{238} Tapola p. 201
rather than refusal to enforce a foreign arbitral award, then it is rational to apply public policy as a ground for refusal.\textsuperscript{239}

This analysis shows that there exist mechanisms that would in theory guarantee that a) no review on merits happen, b) public policy is applied narrowly. In practice, in many cases that are parties (and often debtors in bad-faith) who raise defense of public policy, and they are likely to appeal the rulings in the court. The further discussion will show that mala fide parties tend to abuse the system of review of court rulings. As a result, courts do not always interpret public policy exception consistently. The most common mistake of Russian courts is equaling public policy with principles of Russian law, not necessarily exclusively with fundamental principles of the Russian law. In light of this, we will look into what Russian law and court practice mean by fundamental principles of Russian law.

4.3. Applicable principles of Russian law

In foreign countries, breach of substantive public policy is rarely a ground for refusal to recognise and enforce a foreign arbitral award. Recommendation 2(b) of ILA Report states that the court, in order to determine whether certain principle falls under the scope of international public policy, should take into account the international nature of the case and existence of a consensus within the international community regarding the principle in question.\textsuperscript{240} ILA recommends the enforcement court to research the practice of other courts, opinions of commentators and international conventions.\textsuperscript{241} However, as previous discussion has shown us, compliance with such voluntary recommendations depends on the vast range of factors, including aspects of prevailing mentality and actual competence of the enforcement courts.

The reality of Russian case law differs from theoretical provisions of soft law. The enforcement courts consistently consider the fundamental principles of the civil law to be the part of the Russian substantive public policy.\textsuperscript{242} Moreover, Russian civil law is undergoing a major reform that involves rethinking and reshaping principles of Russian civil law. For instance, Article 1 of the Civil Code of the Russian Federation that lists principles of Russian civil law was revised by amendments dates 30 December 2012.

Assessing public policy in light of reference to fundamental principles, in fact, leads to the review on the merits of the dispute. This is common for the recognition and enforcement of both foreign and arbitral awards and awards rendered by the arbitral tribunals located in Russia. UNCITRAL

\textsuperscript{239} Morozova
\textsuperscript{240} ILA Report
\textsuperscript{241} ILA Report
\textsuperscript{242} Kurochkin 2013
Case 640 (the court ruling dated 15 August 2003) states following: “the [Russian] Court of Appeal […] found that the arbitral tribunal violated one of the fundamental principles of Russian civil law...which the state arbitration court equated with a violation of Russian public policy”.243 In that case, the respondent, a Russian joint-stock company, was supposed to make a payment to the plaintiff, a Polish bank, under an award by the Court of International Commercial Arbitration at the Russian Federation Chamber of Commerce and Industry (ICAC at the RF CCI).244 Even though the case dealt with the enforcing an award of an arbitral tribunal located in Russia, there is still a risk that same tendencies may spill over to the enforcement procedures regarding foreign arbitral awards.

There is no close-ended list of what falls under fundamental principles of Russian law. The scope of supramandatory national norms is not defined strictly. Russian researchers highlight that only court proceedings when court interpret the national norms can help us to determine this scope.245 It is obvious that the substantive and procedural laws of the Russian Federation establish the principles of the Russian law. However, principles can also be found in documents of strategic planning – federal strategic planning programmes, different strategies, decrees of the President and the Government that may directly or indirectly influence the court rulings.246 Even for a local legal counsel, knowing the substance of the whole set of bylaws is a challenge. For a foreign party, it is difficult even to evaluate the vague hierarchy of some categories of bylaws.

First of all, let us turn to the analysis of compound elements of substantive public policy on the basis of comparative legal research. Both legal theory and current legislation provide definition of fundamental principles of Russian law as compound elements of the Russian public policy. According to Zaitsev, by fundamental principles one should mean basic key ideas of law that reflect and determine its essence. This definition is factually identical to the definition of any principle in the theory of law.247 Yakovlev equals public policy to the fundamental principles of the Russian law.248 Tarasov sees the fundamental principles of Russian law is an expression of internal public policy of the Russian Federation.249 Komarov believes that public policy does not include all legal norms, but only norms that regulate foundation of the state, that is norms directly stated in the Constitutions (e.g. provisions on rights and freedoms), or norms based on the constitutional principles. One cannot count social-economic factors as public policy as they are

243 Wires p. 22
244 The court ruling of the Federal Commercial Court of Moscow District dated 15 August 2003 (case No. KG-A40/5470-03P)
245 Sadikov pp. 82-83
246 Kurochkin 2013
247 Tarasov
248 Skvortsov & Yarkov
249 Tarasov
temporary, subjective and locally limited. However, we can see that the researchers do not tackle the risks of such a wide interpretation of public policy and do not address it in interaction with international standards of substantive public policy. From our point of view, such comparisons are vital for the effective evaluation of the wideness of substantive public policy concept and assessing risks of its review on merits. To achieve this comparison, we should look into the practical content of the Russian fundamental principles.

The Civil Code of the Russian Federation refers to general principles. Namely, Article 1 of the Civil Code (as revised by amendments of 30 December 2012) lists following principles: equality of participants in the relationships regulated by it, the inviolability of property, the freedom of agreement, the inadmissibility of anybody's arbitrary interference into the private affairs, the necessity to freely exercise the civil rights, the guarantee of the reinstatement of the civil rights in case of their violation, and their protection in the court. Some courts also invoke the “principle of lawfulness” as a fundamental principle of the Russian law, referring to Article 15(2) of the Russian Constitution, which provides that all state and municipal authorities, officials, individuals and their associations must abide by the Russian Constitution and laws. There are also principles not embodied in legal rules, namely, remedies proportional to the consequences of the breach of obligation and civil liability based on fault. These principles are, in fact, formed by case law as further discussion on case studies will show.

The enforcement courts have been readily referring to fundamental principles of Russian law when defining public policy concept for a long time. Namely, Paragraph 29 of 2005 Information Letter used fundamental principles as a basis for defining substantive public policy. It stated that the Russian public policy is based on the principles of equality of parties in civil-law relations, integrity of their behavior, proportionality of civil liability measures to consequences of contractual breach and a guilt. This approach is also evident from the case law, for instance, the Ruling of 17 August 2012 No. VAS 7805/12 in case No. A56-49603/2011 where the Supreme Commercial Court of the Russian Federation defined public policy in the light of aforementioned principles. Even though that case dealt with the enforcement of the foreign court ruling (namely, of the District Court of Limassol, Cyprus) in a dispute between Fringilla Co. Ltd. and LLC Ryphrominvest on the loan agreement, the reasoning is still relevant for determining general enforcement moods of the courts. As we have discussed in the previous chapter, the Russian

---

250 Kisevela p. 4
251 Davydenko & Kurzynsky-Singer p. 217
252 Davydenko & Kurzynsky-Singer p. 227
253 Karabelnikov 2006
254 Tapola p. 197
courts tend to fail to distinguish between national and international substantive public policy when deciding whether to recognise and enforce a foreign arbitral award. This makes relevant the research of the court rulings on recognition and enforcement of awards rendered by Russian internal arbitral institutions that face a stricter standard of review regarding compliance with the public policy.

The more concrete public policy formula is, the easier it is for a judge to apply it. However, public policy has laconic formula, and how these formula will be interpreted and applied depends on the opinion of the judge.\textsuperscript{255} The discussion in previous chapter has shown that this opinion is formed inter alia by the mentality of involved stakeholders. This is evident from the approach of enforcement courts on defining substantive public policy. Russian courts tend to provide extensive definitions of public policy when applying public policy exception in practice. The SCC in one of its cases stipulated that a foreign arbitral award violates the Russian Federation public policy if its enforcement leads to actions that are “expressly prohibited by the law, damage the sovereignty or security of the state, affect the interests of major social groups, are incompatible with the principles of economic, political and legal system of the state, affect constitutional rights and freedoms of citizens and contradict the major civil law principles such as equality of the parties, inviolability of property, freedom of contract”.\textsuperscript{256} We would like to highlight that the stylistic framing of this definition itself opens the door for a wide interpretation of substantive public policy. Especially, the wording of “incompatibility with the system of the state” and a reference to an open-ended list of “major civil law principles” suggest the readiness of the enforcement courts to widen the concept of substantive public policy. Some principles in practice have such a wide meaning that they can pose a big risk for the recognition and enforcement of foreign arbitral awards.

Especially, the principle of lawfulness shall be approached with caution. The arguments that principle of lawfulness are breached can in fact result in the review of the merits of the arbitral award, which is forbidden under Russian law.\textsuperscript{257}

Usoskin has analysed inconsistency in practice of partial enforcement of arbitral awards. The Supreme Court has confirmed possibility of the partial enforcement of an award granted by an international tribunal located in Russia (Maritime Arbitration Commission at the Chamber of Commerce and Industry of the Russian Federation) if it violates public policy partly. In this case, the court confirmed that enforcing insurance compensation covered by unconditional franchise

\textsuperscript{255} Pavlova
\textsuperscript{256} Baker & McKenzie 2011-2012 pp. 394-395
\textsuperscript{257} Kurochkin 2013
violated Russian public policy. However, enforcing the difference between the full sum and the sum of unconditional franchise does not breach Russian public policy. The Supreme Court ruled that partial enforcement would help to reach the balance of interests of parties and prevent the breach of the principle of lawfulness. There is much less clarity on how partial enforcement will be approached by the commercial courts in case of enforcement of foreign arbitral awards, even though Recommendation 1(h) of the ILA Report highlights the importance of striving for partial enforcement. This unclarity stems from the lack of case law in this field.

Sometimes, public policy is randomly confused with independent grounds for refusal (for instance, absence of notice of the party). Courts explicitly state that there shall be compliance with the clear division line. Unpredictable widening of public policy concept can undermine trust in Russian legal system and decrease stability of economic relations. From our opinion, this goes in line with international standards on distinction of grounds for refusal to recognise and enforce foreign arbitral awards that we have analysed in the first chapter.

This discussion has shown that understanding of fundamental principles of Russian law is essential for predicting possible risks of surprising and unpredictable interpretation of public policy. This understanding equips us to shift to practical case study research covering different stages of development of contractual relationships.

4.4. Case studies: introductory notes

This chapter examines notable cases that dealt with public policy exception for the time range 2007 – 2015. Taking this period as the object of the analysis will help us to trace how practical implementation of two information letters (see 3.4.2) on public policy was developing. In addition, recent cases illustrate the consequences of commercial court reform on the trends in enforcement of foreign arbitral awards. We describe some cases dated earlier than 2007 as the brightest illustrations of misinterpreting public policy exception. These cases provide us with good comparative material and understanding of unlikely, but still possible risks of too wide interpretation of public policy.

This chapter starts with the analysis of the illegality of underlying transactions as a possible violation of public policy. Even when contract is seemingly legal, its breach may still result in severe consequences for the defaulting party. For this reason, we will analyse next how courts consider excessive damages as a possible threat to public policy. Then, we move to exploring

258 Usoskin p. 17-19
260 Opalev
how violation of specific requirements of different spheres of law. Finally, we will look into cases that do not fall under aforementioned categories but still serve as a good illustration of varying approaches to public policy exception.

In each case analysis, we pay attention to highlighting the risks that this case illustrates. A counsel should study the unpredictable reactions of the courts in order to be capable of anticipating and preventing those quirks from scuttling enforcement.\(^{261}\) However, in practice, it is not that easy. Asoskov has reasonably highlighted that the striking majority of the rulings of the supreme instances of Russian state court focus exactly on what does not fall under the category of public policy violation.\(^{262}\) Not even the supreme instance is always successful in applying public policy exception correctly. In fact, Muranov believes that many lawyers can find grounds for criticising the SCC for the shallow thinking, unwillingness to tackle complicated issues, twisting facts of real cases and taking things out of context.\(^{263}\)

Russian legal theory and case law have set general standards of recognition and enforcement of foreign arbitral awards. A foreign court can apply public policy exception, first, if norms comply with norms of international public order, for example, they are targeted against corruption or asset stripping, and, second, in cases of fundamental breach of rights of a debtor or an indefinite number of people.\(^{264,265}\) This shows that the Russian courts strive to comply with international standards of public policy enforcement. ILA Report provides the most uniform guiding principles that include following requirements:

- principle of the finality of arbitral awards (Recommendation 1(a));
- principle that the enforcement court should take into account location of the arbitration seat when assessing whether an award confirms with international public policy (Recommendation 1(d));
- the obligation of the court to set out in detail the method of its reasoning and the grounds for refusing recognition or enforcement in order to promote more coherent practice (Recommendation 1(g));
- principle of separability of the unenforceable part of the award from the enforceable part in order to refuse that part of an award that does not violate international public policy (Recommendation 1(h));

\(^{261}\) Spiegelberger p. 356
\(^{262}\) Zhiltsov
\(^{263}\) Shinyayeva
\(^{264}\) Pavlova
\(^{265}\) The Ruling of the SCC Presidium dated 13.09.2011 No. 9899/09
the obligation of the court to refer to fundamental principles within its own legal system, rather than the law governing the contract, the law of the place where contract is performed or the law of the seat of the arbitration (Recommendation 2(a));

the obligation of the court to distinguish between a violation of mere mandatory rules and violation of international public policy (Recommendation 3(a));

the principle that violation of international public policy shall have consequences in form of manifest disruption of the essential political, social or economic interests protected by the rule (Recommendation 3(b)).

In fact, these recommendations are not easy to implement in practice, and cases that we will analyse further in our research do not contain a clear reference to the aforementioned international enforcement standards. We will look into how Russian courts interpret public policy when deciding whether to recognise and enforce foreign arbitral awards. Following case studies are split into thematic categories. First, we will look into how nullity and voidness of agreements on which awards are based may pose a risk to enforcement of an award, especially in light of indirect tactics used by mala fide parties. Secondly, we will look how courts approach interpret the principle of the proportionality of liability. Thirdly, we will look into unpredictable violations of specific branch legislation and complicated issues of determining capacity of the parties. Finally, we will explore miscellaneous cases that illustrate how non bona fide parties use literal interpretation of violation of public policy in their own interest. This case law analysis will help us to systematise main risks that a foreign investor faces in the process of recognition and enforcement of foreign arbitral awards.

It is important to take into account the ongoing commercial arbitration reform in Russia. It priorly aims at regulating domestic arbitral institutions in order to fight against so called "pocket" arbitral institutions. Namely, the prior aim was to combat a practice in which disputes are resolved between the parties by an arbitral institution which is established by one of the parties, or its parent company. Such practice of “pocket courts” poses a risk of infringement of the principles of objective neutrality and fair treatment of disputes.

As of 1 September 2016, two laws signed on 25 December 2015 have come into force: the Federal Law “On arbitration in the Russian Federation” and the Federal law “On amendments to certain

---

266 ILA Report
267 Melnikov & Teselkin
268 Astakhova
269 Ruling of the Presidium of the Supreme Commercial Court of the Russian Federation dated 22 May 2012, as part of case No. A50-5130/2011
legislative acts of the Russian Federation” (for more discussion see 3.4.1). Even though the laws priorly address domestic arbitral institutions, some of introduced provisions are also relevant for our research. Even though it remains to be seen what practical implications the law will have, we should pay special attention to the following changes.

First, since 1 January 2017, the court of first instance shall rule on the enforcement in one month, not in three months as before (Article 243 of the CPC). The aim of legislators was to promote efficiency. In fact, it brings new challenges. As one of the reviews highlights, additional time pressure means that judges will not have sufficient time to develop a full understanding of the parties' submissions, resulting in decisions made on the basis of “subconscious biases”.

Secondly, the reform will also allow non-parties to arbitration to challenge arbitral awards that concern their rights or duties. Namely, the newly introduced Article 245.1 of the CPC regulates how the interested party may dispute recognition of a foreign arbitral award that does not require coercive enforcement. In practice, we believe that such situations will be exceptional but still it is to early to assess it.

Thirdly, now, to make changes in public registries (such as registries of legal entities, registry of real property, registry of shares) parties should obtain a list of execution through the enforcement of an award. Changes may be made only on the basis of a list of execution. This lengthens the whole procedure (Article 43 of Law No. 382-FZ and Law No. 409-FZ).

4.5. Illegality of underlying transactions

Vagueness of public policy is a good field for parties in bad faith to show creativity and interpret even the breach of dispositive norms as a violation of public policy. However, it is important to remember that a transaction that is contrary to law is a separate ground of its invalidity that has a much wider scope than a transaction that is contrary to the foundations of the legal order and morality. Thus, courts should apply public policy provision only if the transaction underlying the award violates foundations of the legal order and morality, and therefore, violates public policy. In other words, claims concerning illegality of underlying transactions shall pass a “fundamentality of breach” test.

270 Ghibradze
271 Panov
272 Panov
273 Grishchenkova 2016
274 Zhiltsov
275 Davydenko & Kurzynsky-Singer p. 224
276 Davydenko & Kurzynsky-Singer p. 225
The reality and actual enforcement practice is quite different. In contrast to western courts, the Russian commercial courts often assist the Russian entities in artificial creation of situations that may be viewed later as a violation of public policy. “Indirect claims” is the most popular tactic in achieving it among tools of “guerrilla tactic”. “Indirect claims” tactic falls under the scope of “guerrilla tactics”. Guerrilla tactics include the complex set of mala fide techniques, impermissible from the view of arbitration community, that aim at either getting a positive (for the respondent) arbitral award, or making it impossible to enforce the negative arbitral award. The indirect claims scheme is simple. A Russian respondent that anticipates an award to be ruled not in his favor initiates a claim by the third party. Most typically the shareholders that are not bound by an arbitration clause initiate it. The aim of this claim is to make the contract void or invalid. If this claim was successful, any subsequent arbitration contract that contradicts this decision on absence of legal force of the contract would constitute violation of public policy. This is based on the principle of binding force of the court rulings under Russian law.

The Russian commercial courts in such cases appear to ignore the tribunal’s determination of the contract’s validity and rely on the Russian corporate law in their decisions. Therefore, for a foreign investor, it is important to base calculations of risks on details and pitfalls of Russian legislation. At this moment, with the help of isolated cases, we cannot predict whether situation with obviously mala fide indirect claims will ever improve. In case Baltiysky zavod v. Stena RoRo, shareholders of the Russian Baltiysky zavod claimed that by concluding a profitable contract the Swedish Stena RoRo had abused its rights, and thus that the contract governed by Swedish law should be declared void under Russian law. This argumentation was supported by the commercial courts of three instances, evidencing the ever-growing potential of the tactic of “indirect claims”. Karabelnikov highlights that this case has shown the importance of good faith behavior of parties. Presidium of the SCC has evaluated behavior of the defendant who was concealing doubts regarding the validity of acts until entering into the court proceedings as breaching the principles of bona fide. It stated that the lower courts held Baltiysky Zavod's management guilty of unfair practices. However, they failed to establish that there had been collusion between Baltiysky Zavod's management and Stena RoRo, or that Stena RoRo was aware of such practices. The violation by Baltiysky Zavod's management of the obligation to act reasonably and in good faith in the interest of Stena RoRo was not in itself a ground for ruling.

---

277 Khvalei p. 335-336
278 Karabelnikov 2016 pp. 73-74
279 Baker et al. p. 8
280 Karabelnikov 2011 p. 56
281 Karabelnikov 2011 p. 56
282 Karabelnikov 2013 p. 408
on the invalidity of the managements’s acts. Similarly, the low contractual price and the later realisation that the contracts were unprofitable did not indicate that Stena RoRo abused its rights when entered into the agreements.\(^\text{283}\) Therefore, there is no violation of public policy in this case.

Case *Ciments Francais v. OAO Holding Company Sibirskiy Cement* is another iconic case in this sphere. On 4 February 2009, the decision of the general shareholder meeting of Sibirskiy Cement that included approval of a major transaction was considered void, making it impossible for the company to perform its obligations under the contract with Ciments Francais. The Turkish arbitral tribunal ruled in favor of Ciments Francais.\(^\text{284}\) Under this award, Sibirskiy Cement had to pay the damages for failing to perform the contract and option agreement, arbitration expenses and the interest on the illegally borrowed funds. Sibirskiy Cement, not willing to pay this debt, filed a claim with the Russian commercial court. It appealed to the principles of freedom of contract, equality of parties, good faith and proportionality of measures of civil liability. From our point of view, that is a vague and broad range of principles. The defendant believed that enforcing and award in this case would breach all these principles. The court pointed out that the procedure of approval of transactions is aimed at protecting rights of shareholders and cannot result in the breach of rights of the counterparty.\(^\text{285}\) After repeated quashing of judgments of commercial courts of three instances, Sibirskiy Cement finally prevailed. The Russian courts first put on hold enforcement pending resolution of the “indirect claim” and subsequently the claim for invalidation of the main contract was granted. This made enforcement impossible.\(^\text{286}\)

This case shows how the court explored the contractual balance of rights of parties when addressing mala fide behavior of the party.

Another case where OJSC Holding Company Sibirskiy Cement was involved is also relevant for our research. Case *ING BANK N.V., London Branch v OAO Holding Company Sibirskiy Cement*, *ING BANK N.V.* shows that it is problematic for a part to duly prove that transaction in question was fraudulent and therefore it violates public policy. ING BANK N.V. filed a claim with the Commercial Court of Kemerovskaya Oblast to enforce the final arbitral award made in London on 29 October 2011. Under this award, OAO Holding Company Sibirskiy Cement had to pay to ING BANK N.V. the sum amounting to EUR 5,000,328.70; interest rate amounting to EUR 1,000,328.70 for the period from 30 October 2011 to the moment of payment (EUR 876.71 per day), the sum in the amount of GBP 926,694.42, and interest rate amounting to GBP 892,594.98.

---

\(^{283}\) Van der Berg 2012 p. 288-289  
\(^{284}\) Gadelshina  
\(^{285}\) Part 8 of 2013 Information Letter  
\(^{286}\) Karabelnikov 2016 p. 75
for the period from 30 October 2011 to the moment of payment (GBP 195.64 per day). Sibirskiy Tsement objected the enforcement asserting that the agreement, on which the award was based, was in fact a fraudulent transaction aimed at tax evasion in Russia. The Commercial Court dismissed the arguments, stating that likelihood of violation of Russian tax law was not proved. There was no indication that the agreement covered another transaction, as Sibirskiy Tsement never claimed it in previous arbitral tribunal hearings, in contrast, the debtor furnished the evidence on the performance of the obligations under the agreement. That is evident from the text of interim and final arbitral awards.\textsuperscript{287} This case is illustrative for two reasons. First, it has clarified the burden of proof in cases of indirect claims. Secondly, the court has actually analysed the previous behavior of parties in the proceedings to test whether parties act bona fide. This goes in line with Recommendation 2(c) of the ILA Report. It states that “if a party considered that a fundamental principle was being infringed, that party – if it could – should raise it promptly with the tribunal and allow the tribunal the opportunity to address the issue”.

The 2013 Information Letter shows that claiming damages arising from the contract concluded in the result of corruption violates public policy. In criminal case proceedings, the court decided that the contract on which the award was based was concluded under unfair terms. Namely, the representatives of the company were bribing a person that was managing the enterprise. They knew about illegality of the contract. The Russian enforcement court, deciding whether to enforce the award based on this illegal contract, highlighted that fighting against corruption comprises an element of both domestic and international public policy. Namely, this can be evident from a range of international treaties aimed at fighting corruption (the United Nations Conventions against corruption 2003, 1999, OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions 1997). As a result, the court decided that enforcement of a foreign arbitral award resulting in enforcing damages under the unperformed contract concluded as a consequence of bribery violates public policy.\textsuperscript{288} This court ruling complies with the international trends stated in Paragraph 32 of the ILA Report. The paragraph states that “bribery and corruption are generally considered to be contra bonos mores, and most courts will refuse to uphold agreements relating to corruption even when the parties and the acts of corruption are all foreign”.

There is no guarantee that in case with invalidity of transactions the courts will grant partial recognition and enforcement. For instance, courts of the Moscow District refused to enforce an arbitral award, stating that agreements under dispute in arbitration were considered invalid by

\textsuperscript{287} The Ruling of the Commercial Court of Kemerovo Region dated 20 February 2012 (case No. A2716215/2011)

\textsuperscript{288} Part 2 of the 2013 Information Letter
Russian state courts. The foreign creditor stated that only one of the agreements was invalid while the other was valid. However, the Russian courts declared that the partial enforcement of the arbitral award based on the valid agreement was impossible as far as this would lead to another decision on the case. As a result, recognition of the whole award was refused.289 ILA Report in paragraph 37 sets the standard for partial enforcement. Namely, it states that separation of offending parts from non-offending parts, where possible, would not breach the NYC. The practice shows that the courts still do not undertake enough assessment in deciding on partial enforcement.

Case **Yukos Capital S.A.R.L. v OAO Tomskneft** is another good illustration. Both parties once were subsidiaries of the Yukos Oil Company that entered into a loan agreement in 2004.290 The court of the first instance refused to enforce an award of International Arbitration Court at International Trade Chamber of WTO regarding the loan agreement. The court dismissed the claim, stating that the loan contract (on which arbitral award was based) was entered into to cover the transfer of assets that previously had been unlawfully taken from the borrower. Namely, it stated that financing of Yukos Capital for the aim of loans provision happened at the expense of funds previously transferred from OAO Tomskneft by the use of transfer pricing. Thus, the loan agreements on which the award was based were aimed to cover the return of funds to OAO Tomskneft that were illegally confiscated by the use of transfer pricing in favour of other organisations of the holding. Therefore, these loan agreements violated Russian public law, constitutional fundamentals of the Russian state and thus, also public policy.291 Yukos Capital S.A.R.L. asserted that the loan contract was not covering any other transaction. However, the Federal Arbitration Court of the West Siberian District upheld the previous judgment and did not change its reasoning.292 Draguiev sees the case an illustration of forum shopping, namely, a “shopping” of enforcement in a reputable jurisdiction. He highlights that the actual purpose has not been not to execute decision in Ireland after attempts to enforce it in Russia failed but to use the Irish decision on enforcement to support enforcement in another jurisdiction where the “real” execution should take place.293

Case **Traviata Environmental Ltd. v OAO Rosgazifikatsiya** dealt with the enforcement of LCIA award. The award was based on the agreement that was deemed null and void by the Russian


290 Draguiev

291 The Ruling of the Commercial Court of Tomsk Region 7 July 2010 (A67-1438/2010)


293 Draguiev
courts as it was breaching Articles 78, 79 of the Russian law “On the open joint stock companies”. Namely, requirements on getting approval of the board of directors (supervisory board) of a company or the general meeting of shareholders for entering into a major transaction were breached. Under amended law, a major transaction is a transaction that involves an acquisition, disposal or a temporary transfer of possession or use of assets amounting to 25% or more of the total book value of the company assets. It requires a unanimous approval of the Board of Directors. The SCC stated that the courts of the lower instances were correct in refusing to recognise and enforce this award as it violates the constitutional principle of the binding force of court rulings and the public policy of the Russian Federation. In its ruling, the SCC stated following: “During the execution of this decision, any illegal acts can be carried out, or any acts that endanger the sovereignty and security of the state can be performed, that affect the interests of large social groups and that are incompatible with the principles of the economic, political, and legal systems of the state, that affect the constitutional rights and freedoms of citizens, or that contradict the fundamental principles of civil law, such as the parity of parties, inviolability of property, and freedom of contract.” Moreover, this refusal does not threaten neither the coherence of case law in this category of case nor the norms of international law. This case is illustrative for the wide interpretation of public policy as the definition of public policy concept provided by the court operates really vague concepts. The definition of public policy provided by the court corresponds to the public policy concept as it was established by the 2005 Information Letter. Previous research has shown that such a wide definition has already incurred numerous not arbitration-friendly court rulings on recognition and enforcement of foreign arbitral awards.

Case Hipp GmbH & Co. Export KG v OOO SIVMA Detskoe Pitanie shows that it is important to make sure that the courts will not consider arbitration agreement (or arbitration clause) too vague. In 2005, the Austrian company Hipp GmbH & Co. Export KG (Hipp) entered into an exclusive distributorship contract with the Russian OOO SIVMA Detskoe Pitanie (Children’s Nutrition) which arbitration clause referred to the Vienna International Arbitration Center (VIAC) and the Vienna Rules. A year later, Hipp entered into a guarantee agreement with the OOO SIVMA Detskoe Pitanie and the ZAO SIVMA, that made ZAO SIVMA jointly liable for the obligations of the OOO towards Hipp. The arbitration clause of that agreement also referred to VIAC and the Vienna Rules. Under these clauses, an arbitral tribunal ruled an award in August 2009 under

---

294 Kartashkin
295 The Ruling of the Federal Commercial Court of the Moscow district dated 1 July 2013 (Case No.A40-16710/13-68-179. 44)
296 The Ruling on the refusal to transfer the case to the SCC Presidium No. BAC-14549/13 dated 9 December 2013

51
which OOO and the ZAO jointly had to pay approximately EUR 4 271 060, as well as interest and procedural costs, to Hipp. Hipp filed a claim for recognition and enforcement of this arbitral award with the Commercial Court of Moscow on 18 January 2010. A claim was refused and the court stated that arbitration clause in the framework agreement concluded in 2001 did not specify which court had local jurisdiction and moreover was translated vaguely into German. Parties also did not agree which language should apply in case of ambiguities. All in all, the parties had not concluded a valid arbitration clause. In addition, the court held that since there was no principal contract at the moment of conclusion of the guarantee contract, the guarantee contract is null and void. In light of this, the VIAC tribunal did not have a jurisdiction to make an award. The ruling of the Commercial Court of Moscow was reversed on 20 May 2010 on the appeal. The Federal Commercial Court for the Moscow District found that the contract had a clear arbitration clause. As a result, Hipp again requested recognition and enforcement of the arbitral award in the Commercial Court of Moscow on 3 June 2010. However, the Commercial Court this time unexpectedly stated that the VIAC award contradicted public policy. That was surprising because in its first ruling, this court did not refer to public policy. Finally, in June 2011, the SCC ruled that analysing the validity of the contract would mean review of merits that breaches the NY Convention. Thus, courts of first instance and cassation instance had no reasons to refuse enforcement of an award.297 This case shows that the case law remains unpredictable. In fact, Russian lower courts continue to resort to “public policy” in order to prevent foreign arbitral awards from being recognised.298299 The fact that public policy exception may be raised unexpectedly at any stage of court proceeding makes the enforcement process even more unpredictable. This case also shows that it takes long (more than year) to get enforcement in the court of final instance.

Only in 2010, the precedent was created, when the Russian court enforced the award of an arbitral tribunal located in Russia that was based on the agreement that was deemed null and void by the Russian court by the claim of the person who was not a party to the arbitration clause.300 Karabelnikov believes that this ruling has a potential to prevent indirect claims tactic also in cases of enforcing foreign arbitral awards.301 However, such case law is yet to develop.

Moreover, the current reform of the Russian civil legislation gives some grounds for hope that Russian law has sufficient tools to prevent mala fide behavior of parties to the dispute.

297 The Resolution of the SCC Presidium dated 14 June 2011 No. 1787/11 (case No. A40-4113/10-25-33)
298 Wietzorek
299 Nikolayev
300 The Resolution of the SCC Presidium dated 29 September 2010 No. 17990/09
301 Karabelnikov 2013 p. 420
Karabelnikov has discussed how the amendments to the Russian Civil Code dated 1 September 2013 can change the playing field for the users of indirect claims tactics. On the one hand, certain amendments make it more difficult to use these tactics, namely, following revisions:

1. Now the interested parties have a right to ask for consent of management bodies and shareholders to enter into agreements. Also, terms of limitation to file claims regarding major and interested transactions have been shortened.
2. The party is now precluded from disputing the transaction if its will to save the legal force of transaction is evident. This novelty strengthens the principle of good faith.
3. To prove that transaction is null and void, it is not enough just to prove that it contradicts law. The interested party shall furnish the evidence that the transaction violates public interests or rights and interests of third parties that are protected by law.
4. It is now possible to deem the transaction in breach of the company aims under its Articles of Association only if it is proved that the other party knew or should have known about such restrictions in the charter aims of the organization.
5. Also, the decision of the shareholder meeting may not be deemed null and void if the party that claims it has not suffered significant negative consequences of this resolution.

From our point of view, it will take a couple of years before these changes will actually influence the playing field of the recognition and enforcement of foreign arbitral awards. In addition to that, Karabelnikov still argues that some amendments to the Russian Civil Code may actually benefit the users of indirect claims tactic. For instance, under revised Article 166 of the Russian Civil Code, the claimant is entitled to dispute the transaction even though it has not incurred negative consequences from this transaction. Under Article 167 of the Russian Civil Code, the court may decide not to invoke consequences of the invalidity of the transaction if its consequences would be against public order and morality. For instance, these amendments may tackle cases of restitution.\(^{302}\)

4.6. Proportionality of liability

Even though the contract is valid, it still may contain liability clauses that pose a risk for the successful enforcement of a foreign arbitral award. Pavlova highlights that there is no unified approach regarding whether punitive damages amount to the violation of public policy.\(^{303}\) Punitive damages are damages which amount exceeds the amount needed to compensate the

\(^{302}\) Karabelnikov 2013 pp. 426-428
\(^{303}\) Pavlova
individual. Therefore, they are intended to punish the wrongdoer. Enforcement courts are likely to consider enforcement of punitive damages to violate public policy. The 2005 Information Letter stated that the award “should observe the principle of proportionality of the civil law liability to the consequences of the law violation”. It gave a good ground to reject the enforcement of awards on, for instance, treble damages. This provision has raised discussion among commentators. However, we believe that there is another more important ground to address disproportional damages in this context. Namely, the presence of a clause establishing quite an onerous regime is already a strong signal that the debtor will try to escape the liability by appealing to public policy, no matter how progressive and arbitration-friendly current regime is.

From the first sight, it seems that the SCC was supporting pro-arbitration regime. For instance, in the 2006 decision in *Joy-Lud Distributors International Inc. v. JSC Moscow Oil Refinery*, the SCC rejected the Russian party’s argument that the award violated public policy because it was improperly punitive and enforced an award after finding that damages were proportionate to the breach. However, some commentators are more skeptic. They believe that the SCC reliance on the similarity between Swedish and Russian law on contractual penalties raises a question as to whether the enforcement court would have found violation of the public policy if “(i) if Swedish and Russian law were not similar, or (ii) if the Court had considered the penalty disproportionate to the breach of contract”. This proves that reasoning of the courts on the violation of public policy should be studied in conjunction with reasoning regarding other possible grounds for refusal to recognise and enforce foreign arbitral awards.

Paragraph 29 of the 2005 Information letter provides us with another interesting illustration. In described case, the award settled disputes relating to the reorganisation of a joint venture company and the exit of a foreign founding member from this entity. However, the SCC Presidium found that there was no proper contribution to the joint venture company made by the foreign company. Therefore, the Presidium ruled that the enforcement of an award that ordered the reimbursement of such contribution, without settling the fate of the shares distributed in exchange for the contribution, violated Russian public policy, as well as principles of good faith, equality between the parties and proportionality of liability. For this reason, the recognition and enforcement of the arbitral award was refused. This case shows that the court analysed both concrete provisions of applicable laws and general standards of international substantive public policy before ruling on recognition and enforcement of the foreign arbitral award.

---

304 Kulkov p.2  
305 Rothstein p. 5  
306 Ponty p. 449
However, in the case *Kruken GmbH v. Avtodor-Agro*, the enforcement court refused to enforce an award on the ground that the award of damages significantly exceeding the amount of contractual liability violated the public policy of the Russian Federation. The award included annual complex interest rates of 5% (calculated quarterly). In that case, Kruken GmbH filed a claim with the Commercial Court of Kaliningradskaya Oblast to recognise and enforce a FOSFA (the Federation of Oils, Seeds and Fats Associations Ltd) award against OOO Avtodor-Agro dated 6 November 2006. The claim value amounted to the total price of EUR 76,500 (plus interest) and GBP 8,340 of expenses. Federal Apellation Court of Northwestern District confirmed this ruling.

Case Kruken GmbH v. Avtotor-Agro shows the tendency of courts to refer to vague standards. However, in practice, the courts can adopt even a more vague interpretation of standards of public policy. Namely, in the case *Consulting, Management & Contracting Co v. Sylovye Mashiny* two years, the Federal Commercial Court of the North-Western Circuit highlighted that ordering a Russian company to pay interest to a foreign company on the basis of a contract concluded between them did not create “a result that is unacceptable as a matter of the Russian sense of justice”. There is no theoretical discussion of what amounts to the “Russian sense of justice” especially taking into account peculiarities of legal thinking of regional courts. This shows that the courts’ reference to vague philosophical concepts poses a real danger to arbitration-friendly regime in the Russian Federation.

In *Stena RoRo vs Baltiysky Zavod* case, the Arbitration Institute of the Stockholm Chamber of Commerce awarded damages from a Russian company Baltiysky Zavod to a Swedish company Stena RoRo (EUR 20,000,000) caused by the breach of ship construction contracts and an agreement on the optional acquisition of two vessels, as well as legal expenses. The natural step of the debtor (Baltiysky Zavod) was to resist the enforcement of the award in Russia by claiming that the liquidated damages awarded by the tribunal are not known to Russian law and therefore violate the Russian public policy. The SCC stated that “by entering into contracts subject to the substantive provisions of Swedish law the defendant accepted the risks that a relevant public order may encounter rules differing from Russian law regulating similar relations”.

---

308 The Ruling of the Commercial Court of Kaliningradskaya oblast dated 25 June 2008 (case No. A21-8346/07)
312 Krivoi
In case *Odfjell SE v Open Joint Stock Company Sevmash*\(^\text{313}\), the parties entered into three shipbuilding contracts. Sevmash delayed performance of the first contract, and Odfjell rescinded all three contracts. Sevmash returned to Odfjell its advance payment with interest. In the award dated 30 December 2009, rendered by the arbitral tribunal under the rules of the Arbitration Institute of the Stockholm Chamber of Commerce, Odfjell was awarded damages amounting to the difference between the contractual price and the price of the acquisition of substitute vessels. Sevmash argued that the return of advance payment with interest was sufficient compensation and that the damages exceeded the liability agreed by in contract by ten times and thus violated the principle of proportionality and, consequently, public policy. The court of the first instance held that Sevmash in fact demanded the review of the arbitral award on the merits and it failed to show the lack of proportionality of the incurred liability. As a result, Sevmash was ordered to pay the damages pursuant to the arbitral award.\(^\text{314,315}\) This case sets the standard that it is not enough just to claim the disproportionality of the liability. The court would request the claimant to furnish sufficient evidence of this disproportionality. This standard has a good potential to prevent cases when incompetent courts satisfy claims of mala fide parties.

In case *Oil & Natural Gas Corporation (ONGC) v OAO Amur* (case no. A73-1288/2009), the parties entered into a contract concerning the building of a seismic survey vessel. OAO Amur demanded an increase of the contract price due to changes in vessel design. As a result, ONGC rescinded the contract and retained the full amount of the bank guarantee paid by Amur. An arbitral tribunal under the Indian Arbitration and Conciliation Act rendered an award in April 2009. Under this award, ONGC was awarded damages in excess of USD 57 mln. The court of first instance supported the public policy objections raised by Amur. The courts reasoned that the penalties awarded to ONGC representing over 63% of the total contract price were excessive. The court also held that the amount of the bank guarantee (being 10% of the contract price) retained by ONGC was sufficient compensation. In light of this, recognition and enforcement of an award was refused. This reasoning was confirmed by the appellate court and the Supreme Commercial Court.\(^\text{316}\) This case is illustrative as it has assessed the sufficiency of compensation, thus looking into the essence of contractual relationships and fulfilling the universal principle of contractual balance of parties.

Case of *Lugana Handelsgesellschaft GmbH v OAO Ryazanskiy zavod metallokeramicheskikh priborov* is another good illustration. Back in 2005, the German Institution of Arbitration (DIS)

---

\(^{313}\) Case no. A05-10560/2010

\(^{314}\) Butler

\(^{315}\) Van der Berg p. 324

\(^{316}\) Butler
rendered an award, under which Ryazanskiy zavod metallokeramicheskikh priborov had to pay damages to Lugana amounting to USD 463,317.63 plus interest, as well as supply goods in question (electronic devices) and compensate arbitration and legal fees. OAO did not comply with the award voluntarily. Lugana filed a claim with the Commercial Court of Ryazanskaya oblast to recognise and enforce an award.\(^\text{317}\) The court of first instance and the cassation court found that the awarded penalty and litigation costs were breaching the Russian law and thus the enforcement of this part of the award would violate public policy. The SCC reversed these judgments and stated that the way the arbitral tribunal calculated the interest was not violating public policy and, in contrast, illustrated the contractual will of parties.\(^\text{318}\) Also, the courts of the lower instances mistakenly stated that the awards violated public policy in the part of calculating the punitive damages and legal expenses. The foreign arbitral institution has in fact duly analysed all the facts of the case, including the damages clause. Under Russian Civil Code, claiming compensation for the failure to pay off the debts in due time is one of the way to restore the private rights. Moreover, the SCC referred to the SCC ruling dated 19 September 2006 No. 5243/06 that states that punitive damages exist in the Russian legal system and therefore, enforcement of such awards does not violate public policy. This reasoning is in compliance with the dispositive method of private law that states that actions that are not explicitly forbidden are actually allowed.

In another case, Adecco AG filed a claim with the Commercial Court of Moscow to enforce a LCIA award dated 31 October 2010 against OOO Orglot. OOO Orglot objected, stating that the penalty awarded was excessively high and did not correspond to the Russian practice of penalty calculation. The court dismissed the argument, as the respondent failed to prove the clear disproportionality of the penalty to the inflicted damage. The court stated in its ruling that the defendant could have disputed the sum and reasonability of the interest rate in the previous proceedings but failed to do it in a due time. Moreover, English law was applicable in that case. Therefore, references of the defendant to the Russian court practice were irrelevant and there was no violation of public policy. The Federal Commercial Court of Moscow District upheld the judgment stating that OOO Orglot had an opportunity to present his objection to the arbitral tribunal but failed to do so.\(^\text{319}\) We believe that this reasoning stimulates parties to appeal to possible violations of law in due course in proceedings in arbitral tribunal. This would benefit quality of the commercial arbitration and prevent mala fide behavior of parties in consequent enforcement proceedings in the state courts.

\(^{317}\) The Ruling of the SCC Presidium dated 2 February 2010 No. 13211/09 (case A54-3028/2008-C10)
\(^{318}\) The Ruling of the Commercial Court of Ryazanskaya Oblast dated 2 February 2009 (case A54-3028/2008)
\(^{319}\) The Ruling of the Commercial Court of Moscow dated 9 February 2011 (case No. A40118252/2010)
In the case Consulting, Management & Contracting Co v. Sylovye Mashiny, the Federal Commercial Court of the North-Western District highlighted: “the public policy proviso may be used in exceptional cases when application of foreign law could have created a result that is unacceptable as a matter of the Russian sense of justice. In this case, enforcement of the Award of the Zurich arbitration court in the Russian Federation ordering a Russian company to pay interest to a foreign company on the basis of a contract concluded between them does not create such a result”. 320 In that case, a Syrian company asked for recognition and enforcement of an award rendered by the arbitral tribunal of the Zurich Chamber of Commerce under which a Russian company was required to pay the principal debt and also compensation for arbitration fees and expenses for judicial assistance. 321 This case actually shows a positive signal. The wording of previous cases tended to suggest whether the award itself violated the certain notions of public policy. Here, the actual consequences of enforcement of an award are analysed. This approach is in line with worldwide enforcement trends.

During discussions on the draft of the 2013 Information Letter, Kudelich insisted that distancing from the principle of proportionality of liability is a trend evident not only in Russia, but also world-wide. 322 The 2013 Information letter itself gives grounds for positive hopes. It obliges the enforcement courts to assess the punitive character of the damages in each individual case. It clarifies that enforcement of damages provision would violate the public policy in limited number of cases. This happens when the size of damages is so high that actual damages multiple times exceed the size of damages that parties could reasonably foresee when concluding the contract. Public policy is violated also when the freedom of contracts is obviously abused (the party abused the negotiation capacities of the counterparty, the contract breaches public interests and interests of the third parties.

The literature barely addresses the cases of the partial enforcement of excessive damages. For instance, Usoskin highlights that courts can decide on partial enforcement of an award by distinguishing between excessive neustoyka and the rest of neustoyka and thus refusing to enforce only the excessive part of neustoyka. However, he highlights that it may be difficult to

322 Shinyayeva
323 Neustoyka is a form of interest under Russian civi law. Its definition is provided in Article 330 of the Russian Civil Code, the forfeit (the fine, the penalty) shall be recognised as the sum of money, defined by the law or by the agreement, which the debtor is obliged to pay to the creditor in case of his non-discharge, or an improper discharge, of the obligation, in particular, in the case of the delay of the discharge. By the claim for the payment of the forfeit, the creditor shall not be obliged to prove that the losses have actually been inflicted upon him. Text of the Russian Civil Code (as of 8 December 2011) is available at: http://www.wipo.int/edocs/lexdocs/laws/en/ru/ru083en.pdf
decide on this partial enforcement without the risk that this decision will amount to the review of the merits of the case.\textsuperscript{324} It shows that each case of partial recognition and enforcement should be approached individually.

To sum it up, the SCC has developed a detailed standard for evaluating admissibility of punitive damages in foreign arbitral awards. As long as parties with sufficient bargaining power voluntarily enter into the contract that does not violate other provisions of law, assuming different forms and sizes of damages lies in the field of their ordinary commercial risk. However, it comes as no surprise that the defendants are still active in raising public policy exception arguments when they face the perspective of paying “too much”. The lower courts may still interpret public policy broadly in such cases and it will take long to get a pro-arbitration decision on enforcement in the court of the last instance. This situation resembles the cases of claiming invalidity of agreement on which an arbitral award was based as a ground to refuse recognition and enforcement of foreign arbitral tribunals.

4.7. Violation of branch legislation and public policy as a result of enforcement

So far, we have looked into cases that do not require knowledge of specific provisions of Russian law and mostly tackle general ideas of validity of contract and proportionality of liability. The reality is more complicated. In fact, it is difficult for a foreign investor to escape detailed research of Russian law in enforcement cases. Enforcement of a foreign arbitral award may inter alia be refused when results of such enforcement would violate requirements of branch legislation that amount to public policy. Such cases pose special difficulties as for foreign investors it is especially complicated to forecast all risks stemming from details of Russian law requirements. Majority of transactions are regulated by both private and public law. Latter include currency regulations, bankruptcy law and general principles of property law which applicability is difficult to escape in the majority of large transactions.

4.7.1. Currency control

Currency control violations were considered to violate public policy in past. Ukrainian Confectionery Factory A.B.K. petitioned the Commercial Court of the Republic of Kalmykia on recognition and enforcement of a 1999 award against A.V.K. Yug. The court refused the petition. As the defendant complied with award partially, the claimant then applied to the Federal Commercial Court to enforce payment of the remainder (USD 36,166.02). The Federal Commercial Court stated that ordering a Russian company to pay in a foreign currency would contravene Russian public policy. This ruling was reversed by the SCC. In fact, the use of foreign

\textsuperscript{324} Usoskin p. 17-19
currency is allowed as long as currency regulation peculiarities are complied with (namely, Article 140(2) of the Civil Code of the Russian Federation, the Law of the Russian Federation “On currency regulation and currency control”).\textsuperscript{325}

Relaxation of currency regulations has made it more difficult for parties to raise this ground. However, one should be warned that bad faith counterparty may still attempt to use this ground. Case \textit{OOO Cable and Wireless SNG Svyaz v ZAO Zebra Telekom} (case No. A40-81499/10-68697) illustrates that. Even though this case does not concern enforcement of a purely foreign award, we have already discussed that such reasoning of courts regarding domestic awards may spill over cases involving enforcement of foreign arbitral awards. In this case, the Commercial Court refused to enforce an award of the International Commercial Arbitration Court at the Russian Federation Chamber of Commerce and Industry stating that enforcement of a sum in USD under an award would violate public policy. The Federal Commercial Court of the Moscow District cancelled this ruling, stating that the currency regulations in the Russian Federation do not forbid to open and maintain bank accounts in foreign currency between residents and non-residents of the Russian Federation. Moreover, the Federal Commercial Court highlighted that public policy means fundamental norms of economic and social standing of society and fundamentals of the legal order as established by the Constitution of the Russian Federation and federal legislation. The second attempt to ask for enforcement at the Commercial Court of Moscow was successful.\textsuperscript{326} This case shows that despite the general pro-enforcement trends, arguments of parties regarding violations of currency laws may still succeed.

\textbf{4.7.2. Bankruptcy law}

In \textit{Falkland Investments Ltd. v. OAO VBTRF}, the court of appeal refused to enforce a foreign award dated 21 December 1999 (USD 1119379,89) against a Russian company under bankruptcy proceedings stating that such enforcement would contradict the law “On bankruptcy” of the Russian Federation.\textsuperscript{327} Namely, the court stated that under Russian law any monetary claims against a debtor in bankruptcy proceedings may only be filed with the commercial court in the debtor’s region.\textsuperscript{328} It shows that foreign investors should carefully review contractual provisions to ensure strict compliance with mandatory provisions of Russian laws.\textsuperscript{329} Even though this case

\textsuperscript{325} Tapola 2005 p. 339-340 citing the Ruling of the SCC No. 9772/01 dated 6 August 2002
\textsuperscript{326} Karabelnikov 2013 p. 384
\textsuperscript{327} The Ruling of the Federal Appellate Court of the Far-Eastern District dated 4 December 2001 No. Ф03-А51/01-1/2425-а
\textsuperscript{328} Case No. F03-А51/01-1/2425-а (2001)
\textsuperscript{329} Glusker p. 608
is quite old, one should not underestimate the significance of studying peculiarities of Russian bankruptcy law to assess possible enforcement risks.

4.7.3 Principles of procedural law

Case _Apaucuck Point Environmental Limited v OAO Rosgazifikatsiya_ shows that the principle of the binding force of court rulings in certain cases amounts to public policy. In other words, enforcing an award that contradicts a court ruling that has already entered into force would violate public policy. Under a LCIA award dated 7 December 2012, Rosgazifikatsiya had to pay to Apaucuck following sums: USD 2,669,267.24, rate of return in the amount of USD 3,030,454.21 and legal fees and other expenses amounting to GPB 22,752.42. Apaucuck filed a claim with the Commercial Court. The defendant claimed that the award shall be enforced only in that part that does not violate public policy, namely, the part of paying expenses of the investor under the investment agreement, that has not been deemed null and void by Russian commercial courts (in contrast, guarantee agreement was deemed null and void). The LCIA Award was based on the investment agreement and the guarantee agreement, that was deemed null and void by rulings of the Commercial Court of Moscow in cases № A40-151438/09-132-974, № A40-7544/11-131-82 as breaching procedure on approval of major transactions (Article 78, 79 of the Russian law «On open joint stock companies”). The court of the first instance agreed with the defendant. The SCC ruled that courts of the lower instances were correct in refusing to recognise and enforce a foreign arbitral award as this would breach the principle of the binding force of court rulings.330

This case illustrates the need to assess the enforcement risks by studying the history of case law involving the counterparties and knowing the peculiarities of Russian procedural law. This would allow to assess the legal force of court ruling in question and forecast possible implications of court rulings related to enforcement of awards.

4.7.4 Property law

Case _Connyland AG v OOO Mir-disain_ illustrates how the peculiarities of ownership title transfer may shape understanding of public policy violation. Connyland AG filed a claim with the Commercial Court of Moscow to enforce an award of the Arbitration Institute of the Stockholm Chamber of Commerce (SCC) dated 15 May 2012, under which OOO Mir-disain had to pay EUR 522,659.20 and CHF 164,884.16. The enforcement court dismissed the claim stating that the enforcement of the award would lead to violation of public policy. The award provided for the recovery of the sums spent on the modernisation of the purchased item. However, the

---

330 The Ruling on the refusal to transfer the case to the Presidium of the SCC of the Russian Federation No. BAC-15911/13
enforcement court found that the transfer deed had not been signed yet and thus the item was still the property of the respondent. Commercial Court of Moscow ruled that the enforcement of the award would violate rights to private property, to respect of private life, access to justice and fair trial. This decision was upheld by the Federal Commercial Court of Moscow District.\textsuperscript{331} In its reasoning, the court referred to the provisions of the Russian Constitution and Civil Code. It cited Article 1193 of the Russian Civil Code that states that a norm of a foreign law subject to application in keeping with the rules of the present section shall not be applicable in exceptional cases when the consequences of its application would have obviously been in conflict with the fundamentals of law and order (public order) of the Russian Federation. The court highlighted that fundamentals of law consist of fundamentals as established by the Constitution and civil legislation under the Article 1 of the Russian Civil Code (see part 4.3 of this thesis for more discussion on fundamental principles). Moreover, under Article 35 of the Russian constitution, no one may be deprived of property otherwise than by a court decision. Forced confiscation of property for state needs may be carried out only on the terms of preliminary and complete compensation. Article 218 of the Russian Civil Code establishes lawful grounds for acquiring property. From the award it is evident that the purchaser has not become an owner of the amusement park equipment and, knowing that, without lawful grounds and due notification of the property owner, made significant modifications to the equipment. Enforcing an award based on such mala fide behaviour would violate the fundamental principles of the Russian legislation. Therefore, the court of first instance was correct in refusing to recognise and enforce a foreign arbitral award. It is important to highlight that in this recent case the courts were still equating public policy with Russian legislation in its reasoning. That shows that there is still no clear division between international and domestic public policy in the mentality of enforcement courts.

\textbf{4.8. Scope and capacity of parties involved}

The case law shows that the public policy also concerns the legal capacity of parties to the dispute. Thus, practical interpretation of substantive public policy may be influenced by the specifics of the legal status of involved parties.

The 2013 Information Letter stated that the marital property regime establishing procedure for enforcement of debts where the property of one of the spouses may be used to cover the debts (if the funds of the indebted spouse are not enough to cover debts, the debts may be covered by the share of the common marital property the indebted spouse is entitled to in case of division of property) does not violate public policy. This review as based on case \textit{Federalevel Holdings Ltd.}

\textsuperscript{331} The Ruling of the Commercial Court of Moscow No. 68-844 dated 25 March 2014 (Case No. A40-87194/13)
In this case, LCIA rendered an award, under which Ishchuk had to pay a sum of USD 43,426,229.51, GBP 60,881.98 and expenses in the amount of EUR 281,645.74 plus interest. In case in question, the foreign company wanted to enforce a foreign arbitral award against a Russian debtor under the agreement on the sale of shares and options for sale where the debtor was a guarantor, as well as interest and legal expenses. The court of first instance ruled that as the spouse of the debtor was not a party to the agreement, and enforcement of the award would spread over common marital property, this would violate Article 1 of Protocol No. 1 from 20 March 1952 to the Convention for the Protection of Human Rights and Fundamental Freedoms and part 3 of Article 35 of the Russian Constitution. Namely, the Russian Constitution states that no one may be deprived of property otherwise than by a court decision. Thus, the court ruled that enforcement of a foreign arbitral award would violate the public policy of the Russian Federation. The cassation court overruled this decision. Under Russian law (namely, part 3 of Article 256 of the Civil Code, part 1 of Article 45 of the Family Code) the debt of one of the spouses may be recovered through assets belonging to this person. If that assets are not sufficient for recovering the debt, the creditor may ask for the enforcement against that part of the common property that would have belonged to the indebted spouse in case of division of the spousal common property. Moreover, the court pointed out that under part 2 of Article 35 of the Family Code, when the spouse enters into a deal disposing the common spousal property, consent of other spouse is presumed. Thus, there are no grounds to refuse recognition and enforcement of this foreign arbitral award.332 This case shows that it is important to take into account peculiarities of the legal regime of spousal property when dealing with natural persons. These cases may be rare but still fall under the category of disputes with high values at stake.

Case Indosuez International Finance B.V. v OAO AB Inkombank illustrates the risks of dealing with the party undergoing bankruptcy proceedings. Indosuez International Finance B.V. filed a claim with the Commercial Court of Moscow to recognise and enforce a foreign arbitral award against OAO AB Inkombank dated 24 November 2004. The Commercial Court of Moscow stated that enforcing an award would violate the public policy as the debtor had been liquidated and thus the award cannot be enforced. In its appeal, the claimant clarified that it had asked only to recognise the award. The Federal Commercial Court of Moscow District reversed the decision, stating that the unenforceable award cannot violate public policy as it cannot create the consequences unacceptable in Russian law. Thus, the award was recognised but was not enforced.333 In this case, the court of first instance wrongly referred to Article 150 of the CPC of

---

332 Part 9 of 2013 Information letter on the basis of А55-27265/2010 Arbitration Court of Samara Region dated 6 June 2011
333 The Ruling of the Commercial Court of Moscow dated 11 July 2005 (case А40-67836/0488-41)
the Russian Federation stating that court proceedings should stop if the party to the proceedings has been liquidated. Federal Commercial Court pointed out that the claimant and the debtor are parties to the proceedings on the recognition and enforcement of foreign arbitral awards. Thus, under Article 242 of the CPC the claim shall be examined regardless of the liquidation of the debtor. 334 Even though this case does not directly deal with interpretation of public policy, it shows that the risk that court may refer to purely procedural aspects in order probably to avoid the more burdensome task of analysing substance of public policy.

It is also important to assess the risks of entering into transactions with the branches of the companies. Arbitration of Latvian Chamber of Commerce and Industry (LCCI) rendered an award in case OOO Remontno-proizvodstvennoye obyedineniye v OAO RZD. The respondent claimed that enforcing an award would violate public policy as under the award the damages were to be recovered from the branch office of the Russian company that does not hold legal capacity and cannot be a respondent in the dispute. The enforcement court stated that the lack of legal capacity of the company branch is a basic principle of the Russian law and thus the enforcement of the award would violate public policy. 335 This case evidences the need to carefully assess the legal status of Russian legal entities and distinguish between legal status of branches and subsidiaries.

Dealing with companies partly or fully owned by the state poses a special risk. Cases involving entities with state participation illustrate how notions of public policy and public interest are mixed in practice. The Federal Commercial Court of the Moscow Region has also begun to apply a more restrictive approach to avoid re-examining the merits of the dispute. However, cases to the contrary continue to arise, particularly with regard to “high value” disputes against state-owned entities. This distorts the whole enforcement statistics. 336

Public policy is often mixed with the concept of public interest, even though many theorists and practitioners point out that this position is wrong as the public policy prevails over the state policy. 337 Inappropriate mixture of public and private interests demonstrates that Russian commercial courts have not fully abandoned the paternalist attitude of Soviet Gosarbitrazh (a Soviet administrative agency that was responsible for resolving disputes between state enterprises). 338 Now this paternalism is hidden under the guise of defending sovereignty. The

334 The Ruling of the Federal Commercial Court of the Moscow district dated 29 May 2005 No. КГ-А40/2898-05
335 The Ruling of the Commercial Court of Kaliningradskaya oblast dated 21 December 2009 (case No. А2112426/2009)
336 Baker et al. p. 9
337 Pavlova
338 Hendley p.1
courts extend “public interests” to such circumstances and facts which normally are subject only to the discretion of private parties in contractual relationships. Another strategy of reassessing a private transaction from the standpoint of the state’s interests is to refer to broad philosophical categories, such as “social justice” or “legal consciousness” This logic is evident from 2013 Moscow Circuit Court judgment that defines public policy as “those principles of the social order of the Russian state, a violation of which (also in cases of the execution of judgments of foreign courts and arbitration tribunals) could lead to a result that is inadmissible from the point of view of the Russian legal consciousness”.339

*United World v. Krasny Yakor* can be considered as the most illustrative case on violation of Russian public policy. In this case, United World was awarded a sum of U.S. $37,600 against Krasny Yakor the Russian court of first instance granted enforcement. This enforcement decision was set aside by the Federal Commercial Court of the Volgo-Vyatsky Region. It held that enforcement of the arbitral award would lead to the bankruptcy of state-owned Krasny Yakor, which would have a negative influence on the social and economic stability of the city of Nizhni Novgorod, and on the Russian Federation as a whole. Namely, Krasny Yakor manufactured products of strategic value for the security and national safety of the state. Thus, such damages were deemed to violate public policy.340 This case is a good illustration of how state sovereignty spreads onto the entities with the state participation, that is, companies that are only partly owned by the state.

In the case *Energo-Management Anstalt vs Proizvodstvennoye obyedineniye Teplovodokanal*, a German company sought to enforce in Russia an ICAC award against a Russian municipal water and energy public utility for the recovery of EUR 1,230,252.84 and USD 89,442.20. The court refused the enforcement stating that it had been rendered against an entity of strategic importance for the municipality and to the whole region. It ruled that such enforcement would affect negatively the economic and social development of the municipality, and thus the interests of large social groups. This would make recovery of the awarded amount incompatible with the principles of the economic and legal systems of the Russian Federation. The SCC Presidium found no contravention of public policy in this case.341

In theory, under part 2 of article 8 of the Russian Constitution, state or municipal enterprises do not have any privileges when engaging in commercial activities. Russian courts must therefore

339 Antonov p. 331
341 Davydenko & Kurzynsky-Singer p. 211 citing the SCC Presidium Ruling dated 3 February 2009 No. 10680/08.
scrupulously consider applications regarding public policy in cases such as United World v Krasny Yakor, in order to prevent abuse of this principle by a party claiming its preferences in the light of protecting state interests. Foreign parties should stay informed about special status of city-forming enterprises getting acquainted with their founding documents and excerpts from the Unified State Registry of Legal Entities.  

Some judges perceive the task to prevent social and economic "injustices" being perpetrated against Russia as their main role when ruling on enforcement of foreign arbitral awards. For instance, Morozova believes that enforcement in Russia of an award leading to bankrupting an industry which is the main employer in a particular Russian town would be "doubtful." This has led to backlash against arbitration and surprising decisions on enforcement illustrating deeper hostility.

4.9. Mala fide of parties referring to violation of substantive public policy

On 10 August 2011, an ad hoc arbitration in Riga, Latvia rendered an award against OOO Obyedinennaya sudostroitelnyaya kompaniya (Russian company) in favour of Gartic Limited. Under this award, the Russian company had to pay debt in the amount of RUB 200,000,000 and arbitration fees amounting to EUR 3,500. Gartic filed a claim with the Commercial court of Moscow to recognise and enforce this award. The Commercial Court refused the recognition and enforcement stating that it would violate public policy, namely the prohibition of actions directly prohibited by the imperative norms of the Russian legislation, that is, exercise of rights aimed exclusively to harm another person and circumvent law (abuse of rights). In this case, abuse of rights was evident from the failure of the claimant to duly notify the counterparty about the arbitration proceedings and furnish all necessary documents. This case shows that the courts pay increasing attention to assessing features of mala fide behavior in each individual case. Kokorin notes that this decision illustrates the ongoing fight of the Supreme Court of the Russian Federation against abuses of arbitration and the will to create favourable conditions for good faith creditors. They do not need to prove the invalidity of an arbitral award. Expressing reasonable doubts that arbitration really took place would be enough, as the interested party have the burden to prove the contrary.

---

342 Tapola 2005 pp. 331-350
343 Herald Of The Supreme Commercial Court No.7/2000, p.146
344 Pellew
345 The Ruling of the Commercial Court of Moscow dated 3 March 2014 (Case No. A40-170320/2013)
346 Kokorin
Case *OAO Bank VTB v OAO Finansovaya lizingovaya kompaniya* (a finance lease company) illustrates that a typo in the foreign arbitral award that does not influence the content and the meaning of foreign arbitral award cannot be considered as a breach of public policy that would allow to refuse to recognise and enforce an award. OAO Bank VTB filed a claim with the Commercial Court of Moscow to recognise and enforce an LCIA award against OAO Finansovaya lizingovaya kompaniya (OAO FLK) dated 13 September 2009. The claim value amounted to USD 21,913,335.13 plus interest (USD 6,847.92) and legal fees (USD 77,221.29), as well as arbitration expenses (GBP 87.84). The debtor raised the argument that the text of the arbitral award referred to a non-existing letter of a law firm, that was representing the bank, on the basis of which the arbitral tribunal calculated the interest rate to be paid by the debtor. The court of first instance ruled that the typo in the arbitral award referring to the date of the letter by law firm violated Russian public policy and refused to enforce the award. The cassation court stated that the typo was non-significant, it did not change the content and the meaning of the letter and that the arbitral tribunal furnished enough evidence on this typo. Therefore, the court cannot consider this typo to violate public policy as this ground for refusal to recognise and enforce foreign arbitral awards can be used only in the extraordinary cases.\(^{347}\) The cassation court ruled to enforce the award. However, this case shows that the court of first instance may still be prone to the wide interpretation of public policy. It also illustrates that the parties are still ready to manipulate the public policy concept in their own interest. There is a high risk that due to a lack of competence or for some other reasons, the court may accept such arguments. It will take long to get this decision overruled.

In *Sokofl Star Shipping Co. Inc. v. Technopromexport*, the Commercial Court of Moscow denied enforcement on the grounds that the claimant's name was wrongly written (Sokofl Star Shipping Co. Ltd.) in the award and in the time-charter contract that contained the arbitration clause. The court denied enforcement, reasoning that because Sokofl Star Shipping Co. Inc. was not party to the arbitration agreement it was not entitled to enforce the award. This decision was supported in the appellate instance. The SCC, however, held that the question of the agreement's validity was beyond the scope of the court's consideration and cancelled the ruling of the courts of the lower instances that was reviewing the merits of the case.\(^{348}\) This case shows that the review of merits sometimes is effectively prevented only by the court of the last instance, and, in fact, succession in the contract may be a highly debatable issue.

---

\(^{347}\) Part 10 of the 2013 Information letter based on case А40117740/2010 (the Ruling of the Commercial Court of Moscow dated 12 May 2012)

\(^{348}\) Kozmenko & Boog p. 5 citing the Ruling of the SCC dated 13 April 2001, Case No. 5-G01-35.
4.10. Conclusions

This discussion shows us that we can group possible interpretations of violation of public in a number of categories. The most obvious situations may involve claiming illegality underlying transactions and establishing liability in breach of proportionality requirement. These classes have the least evidentiary requirements making them exploitable by bad faith parties.

However, we can observe positive trends. Practitioners note that there is a growing tendency among national courts to take into account principle of finality of an arbitral award. Nevertheless, we shall not discount also other grounds. They pose the most risk, as they expose the foreign parties to the knowledge of specific Russian legislation. In fact, it is especially difficult to predict how the concept of privity of parties will be interpreted as well as their legal capacity in the certain dispute.

The discussion also shows that certain public policy related argumentation may turn out to be unpredictable and tackle a wide range of spheres of law. It also illustrates the will of parties to use wide scope of arguments in their own interest and hope for the lack of competence of a court to make a reasonable and objective ruling. There is a scope of judge discretion but it is reasonably limited by Russian and international case law and doctrines. However, research has shown that it may take years to get an enforcement-friendly ruling in the court of last instance.

The more high-stakes cases reach the Supreme Court, the better picture will emerge of its willingness to reverse anti-enforcement decisions, and the overall state of the foreign arbitral awards enforcement tendencies in Russia. Now, in the view of the practitioners, Russian courts can take a very formal, almost self-serving approach. It happens that “[m]aterial aspects of the case are factored in by Russian courts when dealing with formalities and in reaching decisions by which an application for recognition and enforcement is refused on formal grounds.” This is evident from the most recent cases of years 2012-2013 that dealt with violation of public policy in high-value claims.

5. CONCLUSIONS

The discussion in the thesis has shown that understanding what can amount to the violation of public policy, as well as what consequences it will have, is utterly important. It will guarantee

349 Traspov
350 Pavlova
351 Baker et al. p. 9
352 Glusker p. 610
compliance with due process, improve predictability of business risk and develop trust in investor relations.

In Part 1, we have looked into theoretical grounds and compound elements of public policy. Researching vague boundaries and complex classifications of different kinds of public policy has shown how public policy is prone to change depending on political moods, economic infrastructure and professional competence of stakeholders involved. Therefore, when assessing national experience of interpreting substantive public policy, it is important to understand historical peculiarities and current mentality prevailing in the certain jurisdiction.

Part 2 has dealt with specifics of Russian public policy, stemming from historical specifics, cultural and mentality aspects and the role of different stakeholders in the formation of public policy. It has shown that in analysing Russian case law, it is important to take into account cultural specifics of implementing courts, prevailing mentality of stakeholders, especially Russian commercial courts, and tendencies of the case law in the given region of the Russian Federation.

Part 3 provides an insight into how in practice parties and courts interpret public policy exception in their own interest. We have traced that violations of public policy (or claims of such) may arise at different stages of development of contractual relationships. Moreover, the fate of an award may depend on the knowledge of the peculiarities of the Russian legislation that is constantly changing. Whereas it may be relatively easy to predict the risk that the party may refer to the invalidity of underlying transaction or excessiveness of the liability, some claims may be based on the thorough understanding of specifics of Russian legislation.

On the basis of this, we have come up with some practical recommendations for foreign investors and trade partners seeking to guarantee enforcement of foreign arbitral awards in Russia. Namely, foreign investors should take reasonable precautions when dealing with cases that may result in the need to enforce awards in Russia. Precautions cover the whole lifespan of contractual relationships, namely:

- checking the validity of the contract and identifying the risks that may result in claiming the contract void or invalid at a later stage;
- assessing organisational matters, such as choosing the currency of enforcement, checking contractual documentation for mistakes and typos;
- identifying applicable laws (certain transactions may be regulated by a wide set of requirements of administrative law, and failure to comply with them may be considered as a violation of public policy);
– checking counterparties (especially whether they are undergoing bankruptcy proceedings, are partly owned by the state, and in general have the legal capacity to enter into the transaction);
– checking whether contractual liability meets the proportionality requirement;
– keeping up to do date with general enforcement tendencies in Russia taking into account recent changes into legislation on commercial arbitration.