

ClientAlert

International Litigation

October 2013

Position of the Supreme Commercial Court of the Russian Federation concerning denial of recognition and enforcement of foreign courts' judgments on the basis of contradiction to Russian public policy



On 27 December 2012, a Resolution of the Presidium of the Supreme Commercial Court of the Russian Federation (the **"Supreme Commercial Court"**) No. 7805/12, dated 23 October 2012, (the **"Resolution"**) was published. The Resolution discusses a number of important issues regarding recognition and enforcement of foreign courts' judgments in Russia, including:

- the requirement for the Russian courts to verify that the dispute had a link with the foreign state in the absence of a prorogation clause;
- the possibility of denying recognition and enforcement of a foreign judgment on the grounds that Russian persons were involved in the foreign court's proceedings without their consent; and
- the extraterritorial application to Russian persons' relationships of foreign public law rules prohibiting fraud.

In this overview, we will analyse the Resolution's key findings and its importance for cases concerning recognition and enforcement of foreign courts' judgments and arbitral awards.

Facts of the case

Fringilla Co. Ltd, a Cypriot company (the Lender), entered into a loan for US\$44 million with Rybprominvest LLC (the Borrower). The purpose of the loan was to enable the Borrower and its subsidiaries to acquire equity interests in Russian companies, including in Morskoy Rybny Port LLC (Sea Fish Port LLC). The loan agreement prohibited the Borrower and its subsidiaries from disposing of any assets without the Lender's prior written consent. The agreement was governed by English law and allowed the Lender to commence proceedings in any court having jurisdiction.

The Borrower failed to repay the loan on time, following which it and one of its Russian subsidiaries sold their equity interests in the Sea Fish Port LLC to a third party (a Russian company, Konmark LLC) without the Lender's consent.

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The Lender commenced proceedings in the Cypriot court seeking declarations that the equity interest sale and purchase agreement was invalid; and the consent granted by the Borrower to its subsidiary, allowing it to dispose an equity interest in the Sea Fish Port LLC to a third party, was invalid. The parties involved in the dispute were not registered and did not trade in the Republic of Cyprus. Further, the Russian purchaser of the shares (Konmark) did not agree to participate in foreign court proceedings.

As set out in the Cypriot court's judgment, although the claimant did not name the Russian purchaser as a party to the action, the court sent it a notice of the proceedings and a copy of the statement of claim. The Cypriot court satisfied the claimant's claim on the basis (among others) that the transaction was contrary to a Cypriot law concerning fraudulent transfers of assets.

The Lender filed an application with the Commercial Court of St. Petersburg and the Leningrad Region to recognise and enforce the Cypriot court's judgment. The application was rejected. The Cassation Court affirmed the court of first instance's ruling.

These Russian courts held that the Cypriot court should not have considered the case and doing so was contrary to the public policy of the Russian Federation because (1) there was no prorogation clause in the agreement with the purchaser of the shares and (2) the dispute had no links to Cyprus.

The Supreme Commercial Court agreed to refer the case for consideration to its Presidium. In doing so the Supreme Commercial Court indicated that it was necessary to clarify the legal position in relation to whether it is possible to recognise and enforce in Russia foreign courts' judgments against Russian persons, in the absence of a prorogation clause and a link between the dispute and the foreign court (i.e. *de facto* estimate the foreign courts' decisions on the matter of jurisdiction), when the courts of the Russian Federation do not have exclusive jurisdiction.

The Supreme Commercial Court Presidium affirmed the court rulings issued in this case based on the legal grounds set out below. The Resolution applies retrospectively. Therefore, it will not only be relied on in cases that Russian courts will consider after the Resolution is published, but also in cases that are currently being processed by the courts.

Supreme Commercial Court Presidium's legal position.

Recognition and enforcement a foreign court's judgment concerning a Russian person's rights in the absence of a prorogation clause and a link between the dispute and the foreign state is contrary to the public policy of the Russian Federation

The Supreme Commercial Court found that the denial of recognition and enforcement of the Cypriot court's judgment in Russia was justified. This was on the basis that there was no link between the dispute and the Republic of Cyprus and there was also no prorogation clause.

In addition, the Supreme Commercial Court stated that the judgment affected rights of a Russian company (the purchaser of the shares) "*that did not take part in the court proceedings and did not consent to the foreign court's jurisdiction*". This constitutes grounds to deny recognition and enforcement of the Cypriot court's judgment as "*contrary to the public policy of the Russian Federation, an element of which is the right to litigate*".

The effect of the Resolution is that when petitions are made in Russia to recognise and enforce foreign judgments concerning Russian persons' rights and there are no prorogation clauses, the jurisdictional analysis needs to include consideration of whether there was a link between the dispute and the foreign state, even if the dispute does not fall within the Russian courts' exclusive jurisdiction.

Accordingly, even if the foreign court, under its law (*lex fori*), has jurisdiction to consider the case, the Russian court may deny recognition and enforcement of the foreign court's judgment on public policy grounds, if the Russian court determines that there is no link between the dispute and the foreign state.

These findings are in line with the Supreme Commercial Court's earlier position that when a Russian court determines whether it has jurisdiction to consider a case involving a foreign person, the criteria listed in Article 247 of the Commercial Procedure Code of the Russian Federation may not be formally applied without determining whether there is a link between the disputed relationship and the Russian Federation. For example, when Article 247 of the Commercial Procedure Code was applied in a case involving a foreign person, which had a branch or

representative office in Russia, the Supreme Commercial Court stated that, unless the claim falls within the Russian commercial courts' exclusive jurisdiction and there is a prorogation clause in the parties' agreement, the competent court's ruling needs to be based on the *general criterion of international jurisdiction* as set out in the Commercial Procedure Code – a close link between the disputed relationship and the state.¹

This legal position is also in line with that of the Supreme Commercial Court's Chairman A.A. Ivanov, who stated that bad faith competition between foreign and Russian judicial systems should not be allowed.²

It may also be inferred from the Resolution that a foreign court's judgment needs to name all persons in respect of whose rights the judgment was rendered as formal parties to the proceedings, including all parties to any transaction declared invalid.

Therefore, a foreign court's judgment concerning Russian persons' rights may be recognised and enforced in the Russian Federation only if the Russian persons were parties to the court proceedings; and they either consented to the foreign court's jurisdiction or there is a link between the dispute and the relevant foreign state.

Extraterritorial application by a foreign court of foreign public law rules to Russian persons' relationships infringes on the sovereignty of the Russian Federation and is contrary to its public policy

The Supreme Commercial Court acknowledged that "*extraterritorial application of Cypriot public law... may infringe on the sovereignty of the Russian Federation.*" This provides grounds to deny recognition and enforcement of the Cypriot judgment based on Article 12 of the Treaty between the Union of Soviet Socialist Republics and the Republic of Cyprus on Legal Assistance in Civil and Criminal Matters (the "**Legal Assistance Treaty**").

Such application of the international treaty provisions is not unquestionable. Article 12 of the Legal Assistance Treaty states that "*legal assistance*" (i.e. recognition and enforcement of a judgment) may be denied if it infringes on the sovereignty of the Russian Federation. A similar rule is set out in paragraph 7 of part 1 of Article 244 of the Commercial Procedure Code: the fact that "*enforcement of a foreign court's judgment*" is contrary to the public policy of the Russian Federation provides grounds to deny recognition and enforcement of a foreign court's decision.

However, the Supreme Commercial Court did not assess what consequences the enforcement of the Cypriot judgment in Russia would have and whether such consequences are contrary to Russian public policy.

By recognising that the application by a foreign court of foreign public law rules to Russian parties' relationships (i.e. reasons of the judgment) infringes on Russian sovereignty and is contrary to Russian public policy, the Supreme Commercial Court expanded the scope of these grounds to deny recognition and enforcement of judgments.

Therefore, according to the Supreme Commercial Court's position, extraterritorial application by a foreign court of foreign public law to Russian persons' relationships may be grounds to deny recognition and enforcement of a foreign court's judgment.

This legal position may lead to the following complications.

Certain legal concepts in various jurisdictions fall under private law and public law categories. Moreover, a lot of foreign jurisdictions (for example, common law jurisdictions) are not familiar with the division of the law into private and public. It appears that, pursuant to Article 1187 of the Civil Code of the Russian Federation, a Russian court will assess from the perspective of Russian law (*lex fori*) whether the relevant issues fall within a private or public law category. As a result, recognition and enforcement of a foreign court's judgment may be denied even if, in accordance with the foreign court's domestic law, the foreign court did not apply public law rules.

It is also necessary to bear in mind that a foreign court is not bound by Russian public law rules and it is unclear how it is supposed to resolve disputes involving public law issues. Under its domestic law, a foreign court may well be unable to declare that it has no jurisdiction over such disputes.

It is not rare for foreign judgments involving Russian parties to refer to public law rules. Therefore, there is a significant risk that such judgments will not be recognised and enforced in the Russian Federation and that the Russian court will consider such disputes itself anew.

It follows from the above that the Supreme Commercial Court interpreted public policy broadly in the Resolution. This may result in lower courts denying recognition and enforcement of foreign courts' judgments without valid reason, solely because foreign law rules, that the Russian court thinks are public law rules, were applied to relationships involving Russian parties.

1 Resolution of the SCC Presidium No. 16404/11 dated 24 April 2012.

2 Speech at the plenary session of the Petersburg legal forum in May 2012.
<http://www.arbitr.ru/press-centr/news/speeches/52580.html>

Significance of the case

Given that (as set out in the Commercial Procedure Code) resolutions of the Supreme Commercial Court Presidium in specific cases set a precedent, the Resolution will be of greater significance for cases involving recognition and enforcement of foreign courts' judgments in the Russian Federation.

In the absence of a prorogation clause and a Russian respondent's consent to the foreign court's jurisdiction, Russian courts will have to assess the link between the dispute and the foreign state. On the one hand, this will help to limit the number of cases when Russian persons are involved as co-respondents and the claimant unjustifiably chooses a jurisdiction which is favourable to it (forum shopping). On the other hand, the existence of such grounds to deny recognition and enforcement of a foreign court's judgment (no close link between the dispute and the foreign state) is a matter of discretion, and Russian courts may broadly interpret what constitutes such grounds.

The Supreme Commercial Court's position that extraterritorial application of foreign public law rules to relationships involving Russian persons is contrary to Russian public policy; and it is not required to assess the consequences of the enforcement of the relevant judgment in Russia, may provide grounds to deny recognition and enforcement of foreign judgments and allow the courts broad interpretation.

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