

A CASE OF WINNING THE BATTLE AND LOSING THE WAR: YUKOS V RUSSIAN FEDERATION

INTRODUCTION

On 18 July 2014, the Permanent Court of Arbitration (PCA) in the Hague found that Russia had deliberately expropriated OAO Yukos Oil Company and awarded three former shareholders of the company (**Yukos Shareholders**) approximately USD 50.2 billion.

In early 2015, the Yukos Shareholders commenced their crusade to enforce the three parallel awards handed down by the PCA (**Yukos Awards**). At the same time, Russia brought proceedings before the District Court in the Hague seeking to set aside the Yukos Awards, as well as the three interim awards in which the arbitral tribunal first determined it had jurisdiction to hear the claims (**Interim Awards**). As a result, the war between the Yukos Shareholders and Russia is being fought on two fronts: at the seat of the arbitration where the awards were made, and in the jurisdictions where the Yukos Awards are being enforced.

The most significant battle to date came to a head on 20 April 2016, in the form of a ruling from the District Court of the Hague (**Hague District Court**). In a landmark decision, the Hague District Court granted Russia's application to set aside both the Interim Awards and the Yukos Awards. The Yukos Shareholders and their legal representatives have expressed confidence that the decision of the Hague District Court will be overturned on appeal, however such appeal process may take a number of years. Russia has for the time being won the battle, yet the Yukos Shareholders continue enforcement and recognition proceedings in a total of six other jurisdictions.

In our previous article on the Yukos arbitration¹ we examined complications involved in the enforcement of arbitration awards against States, such as the Yukos Awards, specifically with regard to the 'public policy' exception under the New York Convention² and the operation of the doctrine of 'sovereign immunity'. In this article, we consider the most pressing question at present for both the Yukos Shareholders and Russia: can the Yukos Awards that have been set aside at the seat of the arbitration be recognised and enforced elsewhere? We also consider a question that is more important for the wider international arbitration community: should an award that has been set aside at the seat, be recognised and enforced elsewhere?

THE DECISION OF THE HAGUE DISTRICT COURT

Jurisdiction of the arbitral tribunal

As with other forms of arbitration, in investment treaty arbitration an arbitral tribunal's jurisdiction is preconditioned on there being consent by the parties to submit a dispute to arbitration. Investment treaties often provide general and prospective state consent to the arbitration of disputes with foreign investors.

The Yukos Shareholders brought their claims against Russia under the dispute resolution provisions set out in Article 26 of the Energy Charter Treaty (ECT)³. Pursuant to Article 26(3) of the ECT, each contracting party gives unconditional consent to the submission of a dispute to international arbitration or conciliation.

¹ <http://acica.org.au/assets/media/News/ACICA-Review/ACICA-Review-December-2015-edition.pdf>, page 15.

² Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) (**New York Convention**): <http://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/New-York-Convention-E.pdf>.

³ <http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECTC-en.pdf>, page 80.



The Interim Awards

Russia signed the ECT on 17 December 1994 but failed to ratify it. Russia disputed jurisdiction of the arbitral tribunal on the grounds that it had not ratified the ECT and it was thus not bound by it and had therefore not consented to arbitration pursuant to Article 26. In response, the Yukos Shareholders contended that the entirety of the ECT, including Article 26, applied to Russia on a provisional basis pursuant to Article 45⁴ of the ECT. Russia rejected the position of the Yukos Shareholders, arguing that only provisions of the ECT that did not violate Russian constitution, laws or regulations could be applied provisionally and Article 26 fell outside this ambit.

On 30 November 2009, the arbitral tribunal issued three parallel Interim Awards on jurisdiction⁵. It held that the ECT provisionally applied to Russia from the point of Russia signing the ECT up until it informed the depository in 2009 of its intention not to ratify the ECT. The arbitral tribunal further held that Russian law does not prohibit the provisional application of treaties. As a result, Russia was bound by Article 26 of the ECT, and thus the arbitral tribunal had the requisite jurisdiction to hear the case.

Setting aside the Yukos Awards and the Interim Awards

The issue of jurisdiction was once again at the centre of the Yukos arbitration saga after Russia commenced proceedings before the Hague District Court in 2014 seeking orders to set aside the 2009 Interim Awards and the 2014 Yukos Awards on a number of grounds,

including that there was no valid arbitration agreement⁶. As a preliminary point, the Hague District Court made clear that in set aside proceedings under the Dutch Code of Civil Procedure, an arbitral tribunal's jurisdiction is subject to a full review on the merits.

Contrary to the position taken by the arbitral tribunal, the Hague District Court found that the ECT can apply provisionally to a signatory state but only in respect of those provisions that do not violate the laws of that signatory. It was thus a question of whether Article 26 of the ECT (i.e. the dispute resolution provision) is compatible with Russian law. The court found that it is not; under Russian law, public law matters – of which this dispute is one – cannot be referred to international arbitration. Furthermore, provisionally applicable treaties, such as the ECT, which have not been ratified do not take precedence over Russian law. Accordingly, Article 26 has no legal basis under Russian law and there is thus no valid arbitration agreement between the Yukos Shareholders and Russia.

As a result, the Hague District Court determined that the arbitral tribunal lacked jurisdiction and set aside both the Interim Awards and Yukos Awards⁷.

Appeal and other enforcement proceedings

The Yukos Shareholders have confirmed that they will be exercising their right of appeal to the Court of Appeal in The Hague. Should the appeal go ahead, the Court of Appeal will undertake a full review of the facts and the law. In most cases it is possible to contest the Court of Appeal's decision by appealing in cassation to the

⁴ <http://www.energycharter.org/fileadmin/DocumentsMedia/Legal/ECTC-en.pdf>, page 103.

⁵ <http://www.italaw.com/documents/YULvRussianFederation-InterimAward-30Nov2009.pdf>; <http://www.italaw.com/sites/default/files/case-documents/ita0891.pdf>; and <http://www.italaw.com/sites/default/files/case-documents/ita0411.pdf>.

⁶ *The Russian Federation v Veteran Petroleum Limited, Yukos Universal Limited and Hulley Enterprises Limited* (C/09/477160/HA ZA 15-1, 15-2 and 15-112),

⁷ Upon finding that the arbitral tribunal lacked jurisdiction, the Hague District Court deemed it unnecessary to consider the other arguments put forward by Russia.



Supreme Court of the Netherlands⁸. Thus, any decision to overturn the decision of the Hague District Court could take many months, if not years.

At the time of writing, the Yukos Shareholders have commenced recognition and enforcement proceedings in the United Kingdom, the United States, France, Belgium, Germany and India⁹. The Yukos Shareholders do not appear, at least in the public eye, to have been discouraged by the decision of the Hague District Court. By way of illustration, in their latest filing in the US proceedings, they state the decision of the Hague District Court “has no bearing on the subject matter jurisdiction of [the US court]”¹⁰. The decision of the Hague District Court by no means provides a safe haven for Russia.

CAN THE YUKOS AWARDS BE ENFORCED ELSEWHERE?

As a precursor to the question “should the Yukos Awards, which have been set aside at the seat of the arbitration, be enforced elsewhere?”, it is important to understand the following:

- a) Can an award that has been set aside at the seat of the arbitration be enforced in another jurisdiction and if so, by what means?; and
- b) In what circumstances has this been done?

Can it be done and if so, by what means?

To answer the questions – can it be done and if so, by what means? – it is necessary to look to the New York Convention.

One of the great strengths of international commercial arbitration is the framework for the recognition and enforcement of arbitral awards. Where a party has obtained an arbitration award, that award can be enforced in any of the 156 States that have ratified the New York Convention (**Member States**).

Under the New York Convention, the courts of a Member State may only refuse to recognise and enforce a foreign award on one of the grounds listed in Article V. One such ground for refusal is that “*the award has not yet become binding on the parties, or **has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made***”¹¹ (emphasis added).

It is clear from the wording of Article V that a Member State *must* recognise and enforce a foreign award in the event none of the grounds for refusal set out in Article V apply. However the position is not so clear in circumstances where a ground for refusal exists. In such circumstances, the Member State court is given discretion¹²; it *may not* – but it *may* – recognise and enforce the award.

Furthermore, Article VII(1) of the New York Convention provides that its provisions (including the grounds for refusal set out in Article V) do not “*deprive any interested party of any right he may have to avail himself of an arbitral award in the manner and to the extent allowed by the law of the treaties of the country where such award is sought to be relied upon*”. This ‘more favourable right’ provision allows an interested party to apply domestic rules in respect of the recognition and enforcement of foreign awards where those rules are more favourable than the rules set out in the New York Convention.

⁸ <https://www.rechtspraak.nl/English/Judicial-system/Pages/Courts-of-Appeal.aspx>.

⁹ <http://www.economist.com/news/business/21696960-russia-trying-impede-enforcement-massive-damages-award-baiting-bear>.

¹⁰ <https://s3.amazonaws.com/pacer-documents/36/169200/04515586093.pdf>.

¹¹ New York Convention, Article V(1)(e).

¹² New York Convention, Article V(1) states as follows: “[r]ecognition and enforcement of the award *may* be refused...” (emphasis added). On a plain reading of the language of Article V(1), “may” denotes discretion on the part of the enforcing court.



Thus, the New York Convention, both through the discretionary wording in Article V and the ‘more favourable right’ provision at Article VII(1), provides a means through which a Member State may enforce an award that has been set aside at the seat of the arbitration.

In what circumstances has it been done?

The position is probably most firmly established in French case law. In the leading case of *Hilmarton v OTV*¹³ (**Hilmarton**), the French Cour de Cassation (Supreme Court) affirmed the decision of the Paris Court of Appeal to enforce a Swiss arbitral award in France notwithstanding that it had been set aside in Switzerland.

The Cour de Cassation found, pursuant to Article VII of the New York Convention, the Paris Court of Appeal rightly held that OTV could avail itself of the French rules regarding the recognition and enforcement of foreign awards. Notably, Article 1502 of the New Code of Civil Procedure does not include as one of the grounds for refusal the fact that an award has been set aside in its country of origin.

Significantly, the court made the following observations:

- a) the award rendered in Switzerland is an international award which is not integrated into the legal system of that country, so that it remains in existence even if it is set aside; and
- b) the recognition of an award in France that has been set aside in its country of origin was not contrary to the French conception of international public policy.

The second well-known case is that of *Arab Republic of Egypt v Chromalloy Aero Services*¹⁴ (**Chromalloy**), in which the French position was solidified. This case involved an arbitral award rendered in Egypt ordering the Egyptian government to pay various sums to Chromalloy, an American corporation. The award was set aside in Egypt, but recognised in both the US and France. In enforcement proceedings in Paris, the Court of Appeal echoed the observations previously made in *Hilmarton*, that a foreign arbitral award is an international award which, by definition, is not integrated in to the legal order of that country, so that it remains in existence even if it is set aside.

Interestingly, in *Chromalloy* the US courts refused to give effect to the Egyptian judgment on the basis that (i) the contract between the parties provided that arbitration would be final and binding and could not be made subject to any appeal or other recourse; and (ii) a recognition of the decision of the Egyptian court would be contrary to US public policy in favour of final and binding arbitration of commercial disputes.

The US courts have since gone the other way¹⁵, however in the 2013 case of *COMMISA v Pemex*¹⁶ (**COMMISA**) they reaffirmed their readiness to enforce awards that have been set aside at the seat of the arbitration. In *COMMISA*, the Court found that the Mexican set aside judgment “violated basic notions of justice”, where, in setting aside the award, the Mexican court had relied in part on a Mexican statute that came into effect after the dispute between the parties began.

While the English courts have not enforced an award that has been set aside at the seat, recent English case law suggests it would not be entirely impossible. The English

¹³ *Hilmarton v Omnium de Traitement et de Valorisation*, Cass civ 1, 23 March 1994, ASA Bulletin 1994, page 445. See also, *Pabalk Ticaret Sirketti v Norsolor*, Cass civ 1, 9 October 1984, Rev. Arb. 1985, page 431.

¹⁴ *Arab Republic of Egypt v Chromalloy Aero Services*, Paris Court of appeal, 14 January 1997, Rev arb 1997, page 395 and in *Matter of Arbitration Between Chromalloy Aeroservices, a Div. of Chromalloy Gas Turbine Corp. & Arab Republic of Egypt*, 939 F. Supp. 907 (D.D.C. 1996).

¹⁵ See, *Baker Marine (Nig.) Ltd v. Chevron (Nig.) Ltd* (191 F.3d 194, 196 (2d Cir. 1999)); *Spier v. Calzaturificio Tecnica, SpA*, 71 F. Supp. 2d 279 (S.D.N.Y. 1999); and *TermoRio S.A. E.S.P. v. Electranta S.P.*, 487 F.3d 928 (D.C. Cir. 2007).

¹⁶ *Corporacion Mexicana de Mantenimiento Integral, S. de R.L. de C.V. v. Pemex-Exploracion y Produccion*, 962 F. Supp. 2d 642 (S.D.N.Y. 2013).



courts are not bound to recognise a decision by a foreign court to set aside an award if that decision offends basic principles of honesty, natural justice and domestic concepts of public policy¹⁷. Such position was recently clarified in *Malicorp v Government of the Arab Republic of Egypt*¹⁸ (*Malicorp*).

Can the Yukos Awards be enforced elsewhere?

In light of the above, Russia cannot, and should not, take too lightly the threat of the Yukos Awards being enforced elsewhere. This is particularly the case as regards the French enforcement and recognition proceedings. Outside France, the Yukos Shareholders' prospects of success are arguably lower but are by no means non-existent.

The parties recently aired their respective positions on the Hague District Court's decision in the US enforcement and recognition proceedings. In a filing with the US District Court of Columbia dated 22 April 2016¹⁹, Russia stated, amongst other things, as a result of decision of the Hague District Court, "there is nothing for the Court to confirm or enforce". In their response²⁰, the Yukos Shareholders argued that the decision of the Hague District Court "has no bearing on the subject matter jurisdiction of [the US court] under the arbitration exception to sovereign immunity" and went on to state "it is well-established that courts have the discretion – and thus necessarily the jurisdiction – to enforce a New York Convention award even when the award has been set aside by a foreign decision like the Dutch judgment".

Hold your fire!

In their 27 April 2016 filing in the US, the Yukos Shareholders requested a stay pending the outcome of the appeal of the decision of the Hague District Court.

This is arguably a smart move by the Yukos Shareholders as an appeal of the decision will, as they state in their filing, foreclose "any possible application of Article V(1) (e)" of the New York Convention. However, in reality, any such appeal may take years and is of course not guaranteed to be in their favour.

It will be interesting to see whether the US courts allow the stay and whether the Yukos Shareholders take the same approach in the other enforcement proceedings. Importantly, in *Malicorp*, the judge did not allow a request for a stay pending an appeal of the set aside decision, emphasising that the 'normal approach' is that a set aside decision is treated as final unless and until it is overturned²¹.

SHOULD THE YUKOS AWARDS BE ENFORCED ELSEWHERE?

There are a number of public policy considerations that come into play when considering whether an award that has been set aside at the seat should be enforced elsewhere, including:

- a) Is the court of enforcement challenging the sovereignty or authority of the court of the seat? If yes, should it be?
- b) Does judicial comity come into play?

A related consideration is whether the legitimacy of the review conducted at the seat of the arbitration is so strong that the courts of the place of enforcement must defer to it.

One thing to note with all of the cases referred to above is that the court of enforcement did not openly evaluate the legitimacy of the decision of the court of the seat; it instead focussed on its own laws. For example, in *Hilmarton* and *Chromalloy*, the French court applied

¹⁷ *Yukos Capital SARL v OJSC Rosneft Oil Company* [2014] EWHC 1288 (Comm).

¹⁸ *Malicorp Ltd v Government of the Arab Republic of Egypt and ors* [2015] EWHC 361(Comm).

¹⁹ Notice of Supplemental Authority dated 22 April 2016, <https://s3.amazonaws.com/pacer-documents/36/169200/04515579756.pdf>

²⁰ Petitioner's Response to the Russian Federation's Notice of Supplemental Authority, <https://s3.amazonaws.com/pacer-documents/36/169200/04515586093.pdf>.

²¹ *Malicorp Ltd v Government of the Arab Republic of Egypt and ors* [2015] EWHC 361(Comm) at [28].



the New Code of Civil Procedure. The US and English courts, in *Chromalloy* and *Malicorp* respectively, asked whether the set aside decision was contrary to *domestic* concepts of public policy (although the legitimacy of the decision to set aside may have been an unspoken factor while considering this ground).

Importantly, the recognition and enforcement of set aside awards arguably promotes the creation of “floating awards” i.e. an award that is unattached to any legal system. A claimant is then able to “forum shop” notwithstanding that an award has been set aside in one jurisdiction. This leaves the respondent open to recognition and enforcement proceedings elsewhere. Russia is one such respondent; it may have won the battle, but it certainly has not yet won the war.

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