Russia

SAINT PETERSBURG SEA PORT CASE

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In the spring of 1997, the author's law firm was approached about a case to be heard by the North-West District Court of Arbitration. The case was interesting from a legal perspective, as a dispute between international parties was to be settled on the basis of anti-monopoly legislation, and would have civil law effects.

THE CASE

In 1990, a major company (hereinafter named International Investor) offered to optimize and upgrade the capacities of the Saint Petersburg Sea Port (the Port), which is a key element of the city's and the region's infrastructure. New transhipment technologies, together with advanced container and ro-ro vessel handling techniques, would help boost shipments and trade in the region, give an impetus to a whole number of shipment-related industries, encourage investment and thus increase local budget revenues.

Before the project started, International Investor attempted to negotiate certain guarantees for its new acquisition, ie the right to operate new capacity on special terms that would not be changed for some time, with the aim of recovering the investments early and generate an income. The project's legal scheme envisaged setting up a joint-stock company (hereinafter, the Company) that would receive the Port's appropriate site as a contribution of one of the founders to its statutory capital. The title for the site thus given to the Company would allow it, as provided by its memorandum of association, "to construct, reconstruct, or modernize the port". This provision also put the Company in an exclusive position to obtain future operational income and gave it special privileges as the Port's standing partner, irrespective of the success of the preceding cooperation, construction projects and introduction of new technologies.

It turned out subsequently that International Investor was not keen on making any investments over and above what was nominally required to pay up the modest statutory capital of the newly established Company. It was not keen to pursue the project, but rather to sell its share to third parties at a price incomparably higher than its own paltry contribution. Then, such third parties would be in a better position to make considerable investments in the project.

The Port and other investors, anxious to upgrade the city's infrastructure, were not happy about this. Six years after the Company's Memorandum of Association (hereinafter, Memorandum) was made, no serious work or improvement of the chosen site was evident. As time went by, it became obvious that International Investor, clearly wishing to sell its share in the Company, was also taking its time waiting for the best offer to ➡

be made. In so doing, and exploiting its exclusive rights, International Investor obstructed any attempts by the Port and other investors to modernize the only suitable site of the Port that had been transferred to the Company. Such obstructive behaviour seriously affected the Port's economy, hampered shipments and stunted the expansion of port services.

The Port, contemplating the defence of its rights in this matter, was very conscious of one major legal impediment – all disputes were to be brought before international arbitration in the UK, which promised a lengthy and costly procedure. Following the conclusion of such a procedure in the UK, the arbitration award had to be enforced via a ruling of a court of general jurisdiction in Saint Petersburg. At the same time, the Memorandum's arbitration clause derogated all claims connected with the Memorandum, eg termination, damages, revision, etc. Consequently, any claim filed in a Russian court would be turned down by virtue of article 1, item 3 of the 1958 New York Convention on the recognition and enforcement of foreign arbitration awards, and of the Russian Law On International Commercial Arbitration.

Further, the parties' responsibilities under the project were formalized in a somewhat special way: they were all included in one memorandum – a global and very detailed instrument (memoranda of association normally deal with joint start-up activities and contributions of the parties). There may have been two reasons for this unorthodox approach: the Memorandum was completed in 1991, when Russian corporate legislation was not exactly in order, and this may have compelled the parties to seek legal advice from a country of Anglo-Saxon law. Under typical Anglo-Saxon systems, shareholders enter into broad agreements detailing both basic rights, responsibilities and minor issues of mutual investments, privileges etc.

The Port was limited in its choice of legal remedies on account of several other aspects of the case. The Memorandum – duly registered by the authorities – was set out in such a way that all obligations to invest in the infrastructure of the port were worded vaguely, with no deadlines, amounts or contribution procedures attached. Under the circumstances, it was difficult to present a formal case against International Investor. Although International Investor basically stayed aloof from the Company established specifically for the upgrading of the port and never actually occupied the site suitable for new transhipment facilities, it was legally risky to involve other investors. Since International Investor could sue a new investor for infringement of rights. This potential risk of an international suit deterred other potential international investors, who insisted on cleaning up all – even theoretical – legal issues before committing any form of investment.

PRE-TRIAL ACTIVITIES

Realizing that all claims regarding the Memorandum are covered by the arbitration clause and subject to hearing by a foreign arbitration tribunal, and that any legal action should not result in a lengthy litigation, but rather be swift and effective, the Port and city authorities applied to the Anti-monopoly Committee. Consequently, the Saint Petersburg Court of Arbitration (Arbitrazh) received a claim to nullify those provisions of the Memorandum that contravened the national anti-trust law. The court was requested to invalidate the assignment of exclusive construction, reconstruction and development rights to the Company.

The court of first instance found that the requirement of the Anti-monopoly Committee was justified, and honoured it by ruling null and void the Memorandum's provision that the Company holds exclusive title to the Port's site suitable for the construction and operation of new terminals.

However, International Investor was quick to appeal and the initial court's ruling was revoked by the appellate court, which also provided a detailed and well-structured substantiation of its opinion, leaving no further opportunities to pursue this case, it appeared.

The appellate court's ruling heavily stressed that the Memorandum never caused any damage to any parties, or at least, no damage had never been proven by the Anti-monopoly Committee. In return, the Anti-monopoly Committee lodged an in cassatio appeal to revoke this ruling.

PRELIMINARY ANALYSIS

The review of circumstances and legal analysis highlighted several ways of invalidating the obstructing provision of the Memorandum: it could be achieved through a claim of the third party by nullifying its effect on the future through a judicial procedure, or by challenging the validity of the site's exclusive conveyance in 1991.

In principle, some alternative remedies were also possible in view of the above assumptions. A termination claim based on the failure to "pool efforts and investments for the purpose of introducing new transhipment technologies" would help shun the responsibility to irrevocably grant rights of exclusive use. This approach involved a risk of denial of justice due to the arbitration clause, but it could be worked around: an arbitration clause may not cover termination disputes as they are related to establishing real property titles and are within the sole jurisdiction of courts local to such real property, and holding property title is direct-

ly related to termination prospects (item 3, article 212 of the Code of Arbitration Procedure). It was supposed that the clause on exclusive jurisdiction was subject to extensive interpretation and would not be limited only to replevins or negatory claims, or fact-finding statements.

Other legal remedies included various kinds of owner lawsuits regarding the title for the Port's territory, its reclaiming, rectifying obstructed rights, etc. Still, this gave rise to certain legal difficulties in establishing whether the exclusive rights were actually conveyed from one title holder to another, and whether they could be valid if so vaguely defined, etc.

One other opportunity arose out of the fact that the appellate court based its conclusions on civil law concepts underlying liability – damage to the plaintiff, causation, legal irregularities, and debtor's guilt, whereas the defendant's actions should have been judged by the concepts of public law, special preconditions for action and provisions regarding the defence of public interests exercised by a specialized governmental agency.

This case was special in that, while representing the Port – the defendant in the legal process – as a party to the disputed Memorandum, the author's firm not only supported the plaintiff (the Anti-monopoly Committee), but also helped build its arguments for invalidating certain of the Memorandum's provisions.

The analysis allowed us to see the preference of initial Anti-monopoly Committee claim based on public law together with our additional arguments.

ARGUMENTS PRESENTED BY THE PLAINTIFF

The following arguments were presented in favour of revoking the ruling made by the appellate court.

First, sources of liability in anti-trust and civil law are different. Under civil law, they include illicit actions by a party, damage to property, and causation between the former and the latter. Under anti-trust law on the other hand, both legal and practical actions may in fact be illicit if they lead, or may lead, to an infraction. Therefore, causation is not applicable to them in its entirety – something that the appellate court overlooked.

Secondly, under anti-trust law, an infraction does not result in damages incurred to a single individual or party, but rather that are detrimental to the interests of third parties by way of undermining fair competition. However, the appellate court made its conclusions as if the interests of the Port were the matter in question, and not fair competition and public interests as a whole.

Thirdly, the abuse of dominating position was reflected in by restricting access of potential consumers to this market, as demand for port services and those which can only be provided by making use of port facilities (eg multimodal shipments, export and import transactions, storage, forwarding, etc) was growing, since port capacity was not expanding pro rata to growth in demand.

The abuse manifested itself in restricting market access to shippers and custodians, since port facilities were overloaded.

Fourthly, on the other hand, the abuse was also manifested in that the Port could not use market opportunities by freely choosing building contractors or controlling them properly (replacing existing contractor or hiring new ones, etc).

Further, under Article 18.9 of the Law on Competition, a plaintiff may seek to invalidate any transactions which were not executed by the parties if they involved the conveyance of the rights setting the terms of entrepreneurial activity of the conveying party. The disputed Memorandum (or part thereof) is obviously such a transaction, since it conveyed exclusive rights to develop the only suitable site (exclusive location) for the ro-ro container handling facility (new technology).

Finally, the Memorandum per se constitutes an infringement of antitrust law, as its implementation runs counter to public interests (i.e. those of the state and other economic agents) in that the rights to expand port capacity are conveyed: (1) irrevocably; (2) to a third party; (3) exclusively; (4) for unlimited term; (5) on condition that termination won't affect such exclusive rights for three more years; (6) with a linkage to a location exclusively suitable for the introduction of new transhipment technologies.

Meeting all the above leads, or could lead, to monopoly fees for port services, restricted competition or abuse of market power, which is sufficient for deeming the Memorandum contravening antitrust law.

FINAL JUDGMENT

The judicial proceeding resulted in a judgment in favour of the Anti-monopoly Committee.

Observers believe that the judgment is an important benchmark in Russian judicial practice, since it defended public interests by eliminating unfair competition in the fledgling market for shipping services. This judgment has important social implications, as it created major inroads to the economic modernization of a crucial transportation hub of the north-west region through encouraging foreign investment and major businesses.