

Good morning!

I would like to thank GAR for the invitation to this event, it is honor for me to be here. Certainly, arbitration has become a very popular subject in Russia in recent years, there is an increasing interest of professional legal community in arbitration. Such events as this one are crucial for development of Russian law and I hope that in the future we will have more such high level conferences.

In my short intervention today I would like to focus on two important issues. The first is development of the Russian legislation on arbitration, in particular recent amendments to it. The second is problems that dispute resolution system faces globally, with a focus on investment arbitration.

Turning to the first point, I would like to note that the amendments to Arbitration Law come into force already next week (the 29th of March). This Law introduces the rules necessity of which become obvious during the transitional period of the Arbitration Reform. I would like to draw your attention to the following three innovations:

- 1) First, simplification of rules for foreign arbitral institutions. Now it is explicitly provided that for foreign institutions, wishing to administer international disputes, there is no need to create a representative office in Russia.
This change has already brought positive feedback from the major world arbitration centers. On the 4th of April the Council of the Development of Arbitration will consider the application of Hong Kong International Arbitration Centre. I hope that in the future the number of reputable foreign arbitral institutions willing to enjoy the opportunities provided by the Arbitration Reform will increase.
- 2) Second, new opportunities for corporate disputes in arbitration. There are two points to note: first, an opportunity to consider a dispute based on the corporate agreement when an arbitration clause is concluded not by all legal entity's participants. Also, a new types of corporate disputes now can be administered by the institutions, which have no special rules for corporate disputes, including foreign arbitration institutions.
- 3) Third, now it is the Ministry of Justice, not the Government, which issue final authorization for permanent arbitral institutions. This amendment will reduce time for consideration of applications of arbitral institutions. Foreign institutions could decide not to apply for the relevant clearance for political or other reasons, it is their choice, but is crystal clear now that obtaining of such clearance gives strong competitive strength to foreign institution, applied for it, since their awards are enforced smoothly in Russia. We welcome all distinguished international arbitration institutions to use this advantage, which is important for the parties

having physical assets and business interests in Russia irrespective of the domicile of their legal entities.

We are convinced that these alterations will contribute to development of fair and effective arbitration system in the country. Following this approach, the main objectives of the reform will be achieved, and it will be possible to work on diminishing regulatory mechanisms in the future.

Regarding the development of arbitration in Russia, I would like also to draw attention to the fact that as the result of Arbitration Reform we are witnessing today long-awaited liberalization of legislators' and courts' approach towards arbitrability. Different categories of disputes, which earlier was possible to resolve only in the state courts, have gradually became arbitrable. This is what has happened in Russia for example with corporate disputes and disputes arising from the contracts of publicly owned companies. However, in certain areas the arbitration is still impossible to imagine. Probably, in the future it will be more voices to make more disputes arbitrable as the trust in arbitration is strengthening due to the Reform.

The initiators of the conference announced me as the university professor, so I have a little more freedom to share with you my thoughts and forecasts, and sometimes be provocative.

Each year I start my university course on international arbitration by telling my students that arbitration is best alternative to the state litigation as independent, efficient, predictable mean of dispute resolution. It is also the important factor influencing investment climate and economic development.

But is it still true? Is the arbitration actually a universal way to resolve disputes?

The arbitration, certainly, is an attractive way to resolve disputes for business community, but we should not forget that in all jurisdictions state courts system is developing under the international and constitutional standards, becoming higher and higher.

I dare to suggest that arbitration would have fewer advantages in comparison with the litigation. Proceedings in state courts in many countries becoming faster and cheaper. Of course, this mechanism works only when business has confidence in the courts, believes in justice's fairness.

Today much is being done to increase the attractiveness of the state courts worldwide. In particular, work on the Convention on the recognition and enforcement of decisions of the state courts is currently coming to an end within Hague Conference on International Private Law. This so called «New York Convention for the state courts»

will be opened for the signatures very soon. The Convention will introduce a universal standard of the enforcement of court awards abroad that, certainly, will make litigation in state courts more attractive. With opening of the Convention for signature, which is to be held this summer, the arbitration is under the risk to lose in fact one of its main advantages – recognition and enforcement of the decisions all over the world.

I also would like to stress the importance of the development of a system of state courts in our country. European Court of Human Rights for a long time proclaims that its main objective is to make a system of state courts effective. But, obviously, irrespective of participation in any international organizations, including Council of Europe, it is the obligation of the state under its own Constitution to maintain the high level of protection in national courts, which are responsible for development of the national law, securing rights and freedoms.

Lord Chief Justice of England and Wales in famous Baillii lecture in 2016 expressed an opinion that a consideration of commercial disputes in arbitration “reduces the potential for the courts to develop and explain the law”. He noted that the discussion of legal issues in state court can lead to public debates and, therefore, draw legislator’s attention to some problems. Arbitral awards does not have this effect. Also the confidential arbitration reduces the possibility to know how the law is applied and interpreted. In conclusion of his speech, Lord Chief Justice of England and Wales was straightforward: “it is the courts that develop the law. Arbitration does not.”

The development of the arbitration should not and could not minimize the role of state courts. The unconditional advantage of the latter is the transparency and uniformity of the judicial practice which guarantee a predictability of the law enforcement. It is the effect which the law was designed to achieve.

The state courts became even more attractive as the result of disappointment with a system of the investment arbitration.

In recent 30 years States have been active in concluding BITs, incorporating arbitration clauses in them and thus authorizing investors to refer investment disputes to arbitration. This was mainly done to improve investment environment and attract investments. Nevertheless, no one has figured out positive economic impact from such BITs so far. No one can tell the exact sum of investments raised in economy of, for instance, Russia only by virtue of arbitral clause, existed in its’ BITs. In similar manner, amount of investments that nation attracts owing to BITs cannot be measured. At the same time, we know exactly, that on the basis of one of them the arbitral tribunal rendered an award of 50 billion dollars against Russia.

Furthermore, we know that substantial number of BITs with arbitral clauses has led to vast number of claims that are filed against the states in international arbitration annually. Moreover, statistics indicate, that number of such filings is growing. In the end of 2018 number of known disputes between the states and investors reached 942. If in the 1990s within 1 year in various arbitration centers, including ICSID, between 5 and 10 claims were brought, in the period from 2000 to 2010 an average was around 30 and 40 claims, however just in 2016 investors filed 62 claims against states.

As a consequence, instead of flow of foreign investments, nations get growth of claims against them.

However, matter of concern for the states is not increased number of claims but the fact that functioning of investment disputes settlement system is far from being perfect.

I will name 3 main points.

First of all, it's so-called "pro-investors approach of tribunal and arbitrators". Disputes are initiated by investors. In June 2018 Transnational Institute and non-profit organization Corporate Europe Observatory criticized effectiveness of the Energy Charter Treaty's arbitration, also in light of the bias of arbitrators. In report it was noted that energy-related disputes within the Treaty commonly are heard by the same persons who issued most of the awards in favor of energy companies. Thus, arbitrators secure their appointment to new disputes.

Second, limited number of persons involved in resolution of investment disputes. This leads to the situations, when same persons in different disputes serve as arbitrators, representatives of the parties or experts. As a result, impartiality of arbitrators is called into the question.

And finally, arbitrators' failure to strike a fair balance between economic rights of investors on the one hand and public interest and obligations of the State on the other hand have led to considerable criticism. It seems to me that particularly this point is the most substantive.

Practice of settlement of investment disputes shows that by lodging a claim against the states, investors actually challenging wide range of public policy areas, including environmental policies, public health, labour conditions, taxation, etc. For instance, in 2009 the Swedish firm, holding coal-fired power plant filed a claim against Germany, demanding barely 2 billion dollars compensation for establishing stricter requirements for clean production. These requirements were established in accordance with Germany's decision to reduce air pollution that lead to the global warming. Facing an award of significant compensation, Germany was forced to drop these requirements and let the plant continue working.

Another example of investors' claims, interfering to internal political affairs of states are claims, resulting from adoption by the government of Argentina of the various economic measures in crisis in 2000s, and also tobacco company Philip Morris' claim against Uruguay for adoption of a number of tobacco control laws. You perfectly know all this and other examples. As a result, economic interest of one company prevails over public interest, which is disputable.

In addition to the mentioned points which cause dissatisfaction of the states, there are some disadvantages **of this system for investors themselves**.

They are:

- First, extremely high costs of the arbitration. Expenses are running into millions of dollars. It more and more looks like a classical market bubble, attracting third-party funding, which is often speculative.
- Second, inconsistency and even divergence of the arbitral practice. Very similar legal issues can be decided in opposed manner. It turns settlement of investment disputes into the roulette, where the result depends on the choice of one or another arbitrator.
- Third, inability of arbitration to protect businessmen from the consequences of illegal political sanctions imposed by foreign countries on them.

All named points let down the investment arbitration system both for the states and investors.

As a result of this disappointment, as we know, some countries withdraw from the conventions and BITs that include arbitration clauses.

In 2005 Bolivia denounced ICSID Convention and in 2009 Ecuador followed its example. In 2009 representatives of several states of Latin America, including Venezuela and Nicaragua held a panel discussion in UN offering to close the ICSID. By the 2017 Ecuador has annulled all its BITs, preventing any future agreements contain clauses for settlement of investment disputes in international arbitration. In 2017 India sends notifications to its counterparties about termination of its BITs.

Furthermore, within a context of mistrust to investment tribunals, desire of supranational institutions to restrict competence of tribunals is increasing. It is enough to recall the famous judgement of the European Court of Justice in the *Achmea case*, where arbitration clause from the BIT between the Netherlands and Slovakia, and more specifically mechanism of settling investment disputes envisaged in this clause was seen to be incompatible with Treaty on the Functioning of the European Union. Incompatibility was due to the fact that arbitration award cannot be re-examined by national courts and therefore the tribunal's application of the EU law cannot be

supervised. These award *de facto* makes disputes that arise from about two hundred internal BITs concluded between EU member-states *non-arbitrable*.

Another example is an appeal of the members of the legal community of the USA to limit the sphere of investment arbitration. In October 2017 a group of 230 lawyers and economists addressed the US President with the open letter. They suggested to exclude the investment arbitration from the North American free-trade agreement, and also to abandon this mechanism in the future. As the basis for this suggestion they pointed out, that the investment tribunals substitute the US state courts, often incorrectly interpreting provisions of the constitutional and administrative law, and their decisions are not subject to appeal review, while the opportunity of the review is an important guarantee of the rule of law.

All these examples confirm that today the confidence in international arbitration is under risk. We need reforms in the whole system: developing the transparency of the proceedings, establishing clear standards of proof and evidence rules in arbitration, expansion of number of professionals involved into the sphere, development of due process, making arbitration much more transparent and predictable. All of this is not against the nature of arbitration, rather should help to restore very important confidence of the states and the investors in the international arbitration.

This speech is not to criticize the phenomenon of arbitration, but to try to give more pragmatic view on the problems we face, and try to find solutions. It is frequently claimed that Winston Churchill said that «Democracy is the worst form of government, except for all the others». It is perfectly true for arbitration. Humankind haven't invented anything better than arbitration as transnational dispute resolution system.

So it is very important to hold such conferences as this one, which give the opportunity to discuss openly the existing problems in arbitration. We should also be optimists about developing of arbitration in this country, since we have a young generation of the very talented arbitration lawyers. For example, Russian students won three the most prestigious arbitration competitions in the world recently: Vis Moot, FDI Moot, FIAMC. Certainly, these are considerable victories. They give hope that existing problems can be resolved.

I would also very much welcome all of you at St. Petersburg Legal Forum in May to continue this fruitful discussion.

Thank you!