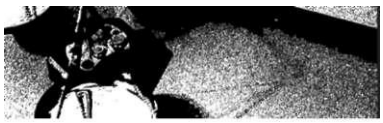

'Arbitration trap' and small claims: Russian recent experience and guidelines

RUSSIA

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This article aims to outline a number of issues that parties are recommended to take into account on 'small claims' matters, both before and after an arbitration begins. These recommendations may help parties to minimise costs and delays and to face these matters 'fully armed'.

In order to avoid disproportionate costs in small claim arbitrations, parties must plan ahead

Recent surveys among large and medium-sized Russian companies show that arbitration has completely won the hearts and minds of those market players. Indeed, some of the enthusiasm may be excessive. More and more contracts, especially with foreign counterparties, include an arbitration clause referring any disputes arising out of or in connection with them to major international arbitration institutions. This includes not only major deals but also more standard contracts, often involving relatively insignificant amounts.

When a dispute arises out of such a contract, and a party commences — or even evaluates the practicability of commencing — an arbitration, it potentially finds itself facing the prospect of arbitration expenses and legal costs that are comparable, and may even exceed, the amount at stake. This has became quite a widespread phenomenon: Russian entities often approach counsel with a view to commencing arbitration against their foreign counterparties before major arbitration institutions to resolve contractual disputes involving amounts in the region of €100,000 to €300,000.[1] Sometimes such disputes involve complex technical issues requiring experts, which entail additional costs. Even where prospects of success are good, it is often difficult for corporate management to accept the budgets required to conduct the arbitration properly.

Certainly, arbitration expenses and legal costs may be recovered at the end of the arbitration if they are awarded against the opponent and the claimant succeeds in enforcing the award. But there can be no certainty of this at the stage when the prospects of success are evaluated. And years may lapse between the date of the claim's filing and the award's enforcement. As a consequence, parties sometimes decide not to commence an arbitration and to write-off the losses because arbitration would simply be too costly and time consuming.

In order not to fall into such an 'arbitration trap', parties should consider in advance the means available to them to ensure that their disputes will be resolved in the most efficient manner.

Clearly worded and carefully thought-out arbitration clauses are crucial

Vague, frivolous or overly complex wording of an arbitration clause can lead to unnecessary difficulties when a dispute arises, and may even create difficulties for enforcement at a later stage. This is particularly the case in jurisdictions where the courts generally take a formalistic approach. For example, in a recent decision a Russian court confirmed the annulment of an International Commercial Arbitration Court of the Chamber of Commerce and Industry of the Russian Federation (ICAC) award because of the arbitration clause's wording: the court concluded that according to a 'strict construction' of the arbitration clause, the parties only agreed to resolve disputes under the ICAC Rules but not to refer them for resolution to ICAC-administered arbitration.[2]

With respect to small claims, a practitioner's usual concern when drafting an arbitration clause and conducting arbitration is to strike a balance between the need to respect due process and the desire for a fast-track procedure. In the case of a simplified process, a losing party may seek to challenge

an award on the basis that they were not allowed to properly present their case.

Such risks may be minimised if an arbitration clause is drafted carefully, in light of the model arbitration clauses provided by international arbitration institutions, and as adjusted to the needs of the particular transaction. Good case management by experienced counsel in the course of arbitration also helps to ensure procedural efficiency and subsequent recognition and enforcement of an arbitral award.

For small claims, a number of options are available

There are a number of options available to parties with small claims, which may make the procedure less costly and time-consuming. Parties and their counsel should evaluate the advantages of each of these options depending on the particulars of the transaction and the types of dispute likely to arise out of it.

When executing an international commercial transaction for a relatively insignificant amount, parties typically base their choice of dispute-resolution forum on two basic criteria: (i) neutrality, as in all cases; and (ii) most critically, speed.

Speed may be achieved by:

- agreeing to a simplified procedure in the arbitration clause;
- referring the case to expedited proceedings; or
- agreeing on fast-track techniques once the dispute has arisen.

Agreeing to a simplified procedure in the arbitration clause

To make arbitration truly fast-track and tailored to the needs of a particular transaction, parties may provide for a number of additional rules in an arbitration clause based on the standard clause of one of the popular arbitration institutions. Thus, the parties may agree in an arbitration clause, inter alia, on:

- the appointment of a sole arbitrator (who will generally be cheaper and faster than a panel of three arbitrators; he/she may also be more flexible as a panel of arbitrators will have to coordinate their schedules);
- limiting the number and volume of submissions (parties may provide for one or, at most, two rounds of submissions, and an additional round in the event of a counterclaim); and
- avoiding or limiting the use of experts (eg, parties may agree to use an independent joint expert).

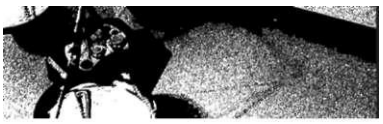
Sometimes parties also agree in their arbitration clauses to limit the duration of the arbitration. Without knowing the circumstances of the dispute, however, it may be difficult to predict in advance the length of time that will be necessary for parties to present their case and resolve their dispute. Accordingly, such a limitation may be undesirable and may even create difficulties for recognition and enforcement. If parties wish to make their arbitrations faster, they may be better advised to impose a limit on the time within which the arbitral tribunal must render its award(s).

Referring the case to expedited arbitration

Some arbitration institutions recommend, for small and medium-sized claims, a model arbitration clause referring disputes to expedited proceedings. This makes it unnecessary to devise a tailor-made simplified procedure in an arbitration clause. For instance, the SCC has adopted the Rules for Expedited Arbitrations which are recommended for minor disputes. Provisions for expedited proceedings are also sometimes incorporated into the arbitration rules: see, for example, the Swiss Rules of International Arbitration. The key features of such provisions are essentially the same as those described above (appointing a sole arbitrator, limiting written submissions, a time limit for rendering the award and the limiting or avoidance of hearings, etc).

Although parties may use different tools to reduce the time and costs of arbitration, the specific procedure provided by certain arbitration rules (which efficiency has been tested by a significant number of cases) may be the preferable choice for small claims. Drafters of standard contracts for the day-to¬ day running of a business who do not wish to spend time drafting arbitration clauses or do not have the necessary experience to do so are recommended to adopt one of the model clauses or rules mentioned above. Unfortunately, the rules of the ICAC, which often handles minor disputes,[3] do not provide for such a special procedure. They merely recommend that parties appoint a sole arbitrator, rather than a panel of three, where the claim does not exceed €25,000.

Another solution may be needed for high-value contracts out of which small claims may arise.



The Swiss Rules automatically refer all claims valued at up to CHF1m (about €800,000) to expedited proceedings, unless the Arbitration Court decides otherwise. Parties, therefore, may include a standard clause in a contract and leave it to the institution to decide whether to have expedited proceedings. Otherwise, they can draft a combined arbitration clause that (i) refers disputes to expedited or full-scale arbitration depending on the circumstances of the claim; or (ii) provides for fast-track arbitration tools (such as the appointment of a sole arbitrator) depending on the amount of the claim.

Agreement on fast-track techniques once the dispute has arisen

Given the ability of parties to agree on procedural issues at any stage, they may choose to include in their contract a standard arbitration clause (ie, without specifying any fast-track techniques) and then try to agree on procedural issues at a later stage (ie, after a dispute has arisen).

However, once a dispute has arisen, at least one of the parties may not be interested in avoiding an overly complicated dispute-resolution mechanism. Accordingly, it is much easier to reach mutual agreement at an earlier stage, when the parties still share a constructive approach to dispute resolution.

This does not mean that parties need to describe every detail of the procedure in their arbitration clause. They need only provide for some basic tools and procedures that may be particularly desirable for minor disputes. Other procedural issues may more conveniently be decided in the course of the arbitration, once the particularities of the dispute are better known. These include:

- bifurcation of the proceedings, which may avoid the need for further proceedings once a decision on, say, jurisdiction or contract validity has been issued;
- avoiding or limiting the scope of discovery and documentary evidence;
- replacing excessive procedural correspondence by holding case management telephone conferences; and
- replacing hearings on procedural issues and/or merits with telephone, or video, conferences.

Using electronic equipment to present the case (instead of hard copies) may also help to reduce costs. This option, however, should be considered in light of the relevant arbitration institution rules and applicable law.

Choosing a good seat will help the arbitration run smoothly

Parties are, in general, free to choose the legal seat or place of arbitration, regardless of the location of the arbitral institution that they may choose. The drafters of an arbitration clause should analyse which jurisdiction would be most appropriate as the seat, taking into account both legal and infrastructure considerations. The arbitral seat may have an impact on issues of procedure, recognition, enforcement and annulment, and the question of support by local courts (eg, in granting interim measures). While parties may agree to designate another location for meetings and hearings in the course of the arbitration (a different location to the formal seat of the arbitration), in many instances choosing the place of arbitration effectively means choosing the location at which hearings and meetings with the tribunal will take place. Accordingly, selecting a place of arbitration that has good facilities, including certain specialists (eg, interpreters), at a reasonable price, can also help the arbitration to run smoothly and efficiently.

Investigating the opponent's assets at an early stage can avoid wasting time and costs

The economic value of an award will typically depend on its enforceability. In order to not waste time and expenses, and in order to ensure that an award will become a genuine asset, a party should gather information about its opponent's assets (both their value and their location) before commencing an arbitration. This is particularly important where the opponent is a non-public company with an unknown ownership structure.

With respect to small claims, the claimant is usually not prepared to follow its opponent all over the world, which is why it is advantageous to perform this exercise before the arbitration in order to have an idea of the steps that will be needed in order to enforce the award. Preliminary investigation may also be useful if a party intends to seek interim measures against its opponent.

After the event insurance may be advisable where there is a constant flow of minor disputes

Although 'after the event insurance' (AEI) is widely used in US and European practice, Russian insurance companies do not offer

such a product and Russian parties do not commonly use it abroad.

In short, AEI is obtained after the dispute has arisen and covers certain legal costs of the arbitration. An insured is usually required to finance the arbitration from its own funds, subject to being able to recover the amounts expended from the insurer (if the claim is unsuccessful) or the opponent (if the claim is successful). The broker's fee may be deferred and payable only if the case is successful.

It may be advisable for a company dealing with a constant flow of minor disputes to consider using this type of product.

Notes

1 The mentioned amount is based on the authors' experience, cited only as an example for the purpose of the present publication and what would constitute a 'small claim' may vary depending on parties and circumstances of the case.

2 See the Decision of the Federal Commercial Court of Moscow Region dated 13 March 2012, case No A40-29251/11-68-256.

3 According to ICAC's statistics, 33 per cent of claims considered by the ICAC in 2011 were for an amount up to US$50,000; see: **www.tpprf-mkac.ru/ru/whatis/-2010-** (in Russian).