INTERNATIONAL

Russian tort law in the eyes of the English courts—Part 1

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Abstract

The article considers application of Russian tort law by English courts in commercial fraud cases, it touches upon such topics as elements of tort, tortious interference and pure economic loss. The article aims to compare whether the approach of the English courts in applying Russian law is consistent with how Russian law applied by the Russian courts.

Introduction

Over the past 13 years, Russian law has become very familiar to the English judges. This is a result of the fact that many commercial disputes between wealthy Russians, in which Russian substantive law is applicable, have been considered by the English courts. Such disputes include well-known disputes between Russian Oil Company Yugraneft and Roman Abramovich (2008), Bank of Moscow and Vladimir Kekhman (2018) and some others.

In the legal press these cases were covered as follows:

- "Russia and Kazakhstan continue to feature prominently in an annual report on the biggest users of London's commercial courts"[1];
- "[I]t is clear from the most cursory glance through the daily list and recent reported cases that many [cases], including many of the most high-profile and high value, involved Russian/CIS parties and/or interests"[2];
- "In the last 15 years, English courts have been flooded with cases originating from the former Soviet Union … most Russian related litigation in London could fall into one of the following three categories: commercial disputes, fraud (including white-collar crime) and family disputes".[3]

Last year, a judgment in another somewhat highly anticipated case, *PJSC Tatneft v Bogolyubov*,[4] was handed down. Tatneft, one of the largest Russian oil companies, claimed US$300 million for tortious acts allegedly committed by the defendants, who are Ukrainian businessmen of big names. Again, the English High Court became a forum for this legal fight. It has been said that "[this trial] … is understood to have been the longest fully remote Commercial Court trial to date".[5] We cannot but cover this case in this article too.

There are many factors explaining the reasons for this state of affairs: starting from the fact that sometimes individual litigants are often residents in the UK, a possibility to obtain a WFO from the English courts as well as a comprehensive disclosure order against an adversary party, and not to mention that the Russian judiciary is not as equipped and prepared to devote significant time and resources to litigants as its UK counterpart. Effectively, the English judicial system renders a tailored legal service for this type of disputes where clients are prepared to throw money and endless resources to get the result needed. But it is one thing to select a proper jurisdiction, and another thing to choose applicable law. Inevitably, English courts often have to apply Russian substantive law to such disputes.

This sometimes create a parallel reality as to what is Russian law as applied by Russian courts within Russia and Russian law in the eyes of the English judges (and this of course comes not without the help of English counsel artfully/ingeniously presenting Russian law points).

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[1] M. Walters, "LAW Russian litigants 'loom large' in record year for London courts" (8 May 2019, The Law Society Gazette online), *https://www.lawgazette.co.uk/law/russian-litigants-loom-large-in-record-year-for-london-courts/5070205.article* [Accessed 1 February 2022].

[2] S. Davenport QC and H. Pugh, "Russian litigation in London (Pt 1)" (22 March 2019, New Law Journal online) *https://www.3harecourt.com/assets/asset-store/file//169%20NLJ%207833,%20p16.pdf* [Accessed 1 February 2022].

[3] S. Litovchenko, "Bivonas Law: Russian Litigation in London" (6 June 2019, Lawyer Monthly online), *https://www.lawyer-monthly.com/2019/05/bivonas-law-russian-litigation-in-london/* [Accessed 1 February 2022].

[4] *PJSC Tatneft v Bogolyubov* [2021] EWHC 411 (Comm).

[5] "High Court Judgment Handed Down In Tatneft" Essex Court Chambers, *https://essexcourt.com/high-court-judgment-handed-down-in-tatneft/* [Accessed 1 February 2022].

When applying Russian law, the English courts, from time to time, interpret differently one and the same legal issues of Russian law entailing uncertainty and inconsistency in the resolving of Russian law issues. This is because the content of Russian law is treated as a matter of fact from the perspective of English procedural law. Therefore, for example, inaccurate or incomplete statements of Russian law experts, or misunderstanding between an expert and a judge, which may exist due to the language barrier, may cause a corresponding inaccurate determination of the content of Russian law.

This evidences that nowadays there exists a problem connected with, in some sense, inaccurate application of Russian law by the English courts having different education and legal background and fully relying on the experts' statements.

Moreover, it appears that the trend towards the litigation in English courts will not decrease in the near future. Indeed, in *PJSC National Bank Trust v Mints*,[6] the court allowed to pursue the claim in England simply due to a possibility/risk that the judgment of a Russian court, if rendered in relation to this dispute, may be subsequently claimed by the defendant in the UK as being improperly influenced/obtained, and what may potentially cause difficulties in its recognition abroad (for instance, in the UK).

With this in mind, in order to highlight some of the recurring themes and misconceptions of Russian law, in this article we want to give a view on some of the noteworthy English cases resolving Russian law issues.

There are many aspects of Russian law that have been considered by English judges so far, but, in our view, the most interesting cases for review are those that concern the application of arts 10 and 1064 of the Russian Civil Code (RCC). These articles deal with the general civil law principle of prohibition of abuse of rights and tortious liability for causing harm. For some unexplained but at the same time unsurprising reasons, these rules of the RCC have featured in the cases where allegations of commercial fraud, corporate raids and dissipation of assets were pleaded.

Given the number of cases we intend to cover and the need to provide an overview of Russian legal background, the article is split in two parts published in two consecutive series. In part 1 we cover the relevant Russian law concepts and authors' view as to how they have been applied by the Russian courts so far. In part 2 we provide a comprehensive overview of the cases heard by the High Court of Justice in which relevant concepts have been considered, but from the perspective of Russian law practitioners.

Controversial issues of Russian tort law

Overview

Russian law, as opposed to common law, enshrines a unified theory of "general delict" which, through a complex network of rules, encompasses common regulation for all torts. In other words, Russian law provides for one article in the RCC only (namely, art.1064, which text is given below) that covers all types of tort (there, however, exist some special rules regarding certain types of torts). This principle establishes that any person is prohibited from inflicting harm to another person or his property, and any infliction of harm to another person is presumed unlawful, unless the law provides otherwise.

This concept is analogous to the French law concept, incorporated in the French Civil Code, to compensation of harm caused. Articles 1382 and 1383 of the French Civil Code provide as follows:

- **Article 1382:**

  "Any act whatever of man, which causes damage to another, obliges the one by whose fault it occurred, to compensate it."

- **Article 1383:**

  "Everyone is liable for the damage he causes not only by his intentional act, but also by his negligent conduct or by his imprudence."

English tort law, in its turn, is comprised of different torts which are based on some "basic rights"[7] that should be *actionable* under the law to receive compensation,[8] since it imposes civil liability for breach of obligations specifically established by law.

Controversial issues in the application of articles 10 and 1064 of the RCC

Considering the content of the "general delict" theory under Russian law, as it is described above, such element as "unlawfulness" of the defendant's conduct has become the key element of tort under Russian law. It governs the legal characterisation of alleged acts as lawful or unlawful and, accordingly, actionable or not.[9] Basically, as a starting point, the unlawfulness is presumed, and the defendant thus should demonstrate that it had a right to cause harm or had a lawful justification for committing such act. If the defendant demonstrates that its conduct was permitted by the law, then it would be the burden for the claimant to prove otherwise (i.e. "unlawfulness" of the defendant's conduct: lack of a lawful justification for a committed act, violation of the law).

[6] *PJSC National Bank Trust v Mints* [2021] EWHC 692 (Comm).
[7] N.J. McBride and R. Bagshaw, *Tort Law*, 6th edn (Oxford: Pearson, 2018), p.5.
[8] McBride and Bagshaw, *Tort Law*, 6th edn (2018),p.312.
[9] First, the "non-actionability" of a tort does not prevent a claimant from issuing a claim under Russian law, since it is up to the court to decide whether a specific tort is actionable or not. Second, there are other elements of tort which can also affect the "actionability" of a tort and which are described below.

But it is a common situation that the acts of the defendant who is alleged to have committed some civil fraud may apparently (prima facie) be lawful (or using the words from one English case discussed below, "payments made in legitimate business transactions are not unlawful, and a person cannot be said to be at fault on that account"[10]). In such a case the possibility of application of art.1064 may seem to have been lost, and one way to protect the victim's interests would be to appeal to a relevant investigative authority to probe for any illegal conduct that apparently was framed as lawful actions, but in reality constituted a crime. This is the first controversial issue under Russian tort low.

To resolve this issue, in recent time another trend has developed which is to invoke the general rules in art.10 of the RCC (prohibiting abuse of rights, which text is given below) in conjunction with art.1064 of the RCC (instead of resorting to criminal investigation or by challenging the disputed transactions which often may not yield any result). How does this approach help?

Article 10 provides for the general principle of prohibition of abuse of rights, and thus it prevents bad faith conduct of the parties to civil-law relations. Particularly, it prohibits the use of legal rights in bad faith manner and not in accordance with a purpose of the corresponding legal rule. In effect, this article creates a civil law sanction for the violation of a duty (obligation) to act in good faith. There is a common understanding that English law is reluctant to imply a general duty of good faith. But in civil law jurisdictions it is a common approach to have such duty in the civil code.

Since abuse of rights constitutes a violation of art.10 (and, accordingly, a duty to act in good faith), which prohibits such conduct, it means that the element of "unlawfulness" may be proved by resorting to art.10 (i.e. if one acted in abuse of rights, he thus violated the rule of law). It means that if a claimant proves abuse of rights on the part of the defendant, he simultaneously proves unlawfulness of the defendant's acts. Thus, an unrestrained civil remedy is used to resolve the issue of characterisation of apparently (*prima facie*) lawful acts.

However, such generous application of both arts 10 and 1064 together paves the way for the second controversial issue of Russian tort law: the uncertainty in commercial relations and unlimited liability of the parties to such relations, since it becomes unpredictable whether a party violates the legislation (and/or someone's legal interests) or not. Article 10 does not provide for any clear criteria which would allow to distinguish acts committed in abuse of rights from genuine non-prohibited acts. Thus, a party to civil relations cannot beforehand figure out whether he abuses his rights or not, since he determines by himself whether he can carry some act, but other persons (a counterparty, a court) would establish whether such act was committed in abuse of rights or not. So the concept of prohibition of abuse of rights is quite broad (if not to say vague as it lacks precision or any defined confines).

We raise these questions because, as it is demonstrated below, English courts are inevitably forced to deal with these issues too. Usually, the commercial disputes are complex, insofar as illegality of the defendant's acts may not be easily obvious, and the claimant may be compelled to resort to the concept of good faith.

Third controversial issue that has also been in the spotlight of the English courts is the notion of "harm" under art.1064. There are different views on it, and English courts had to choose one of them to decide whether a claimant can claim compensation for a specific type of harm caused to it.

Vague notions of "harm" and "abuse of rights" principle together, in the absence of their specific definitions, cause the fourth controversial issue: a right to claim damages for pure economic loss (e.g. for interference[11] in other person's legal relations) and reflective losses (i.e. harm caused to another person but which economically affects the claimant's rights or interests). The issues of pure economic loss and reflective losses are widely discussed in the legal literature, and therefore we do not separately analyse these concepts in detail in this article. But we see repeated attempts to deploy these types of claims before the English courts. So far, they have primarily been unsuccessful, and we consider these cases in this article.

Article 1064 of the RCC

Article 1064 provides as follows:

> "1. Harm caused to the person or property of a citizen and also harm caused to the property of a legal person shall be subject to compensation in full by the person who has caused the harm.
>
> A law may impose the obligation of compensation for harm upon a person that that has not caused the harm. …
>
> 2. The person who has caused the harm shall be freed from compensation for the harm if he proves that the harm was caused not by his fault. A statute may provide for compensation for the harm even in the absence of fault of the person who caused the harm.
>
> 3. Harm caused by lawful actions shall be subject to compensation in the cases provided by a statute. …"

Therefore, the following four elements should be established under art.1064 to hold a person tortiously liable: (a) the existence of harm suffered by the claimant; (b) that an unlawful act was committed by the defendant; (c) the existence of causation between the act and the

[10] *Fiona Trust v Privalov* [2010] EWHC 3199 at [94]–[95]; this case is discussed further below.
[11] "Tortious interference" as a common law tort was not taken into account in preparation of this article, since there is no such separate type of claim under Russian law.

harm; and (d) the existence of fault of the defendant. Only the first two elements are relevant for the purposes of this article which we consider below.

Article 10 of the RCC

Article 10 provides as follows:

> "1. Exercise of civil-law rights exclusively with the intent to cause harm to another person, actions in evasion of the law with unlawful purposes, and also other exercise of civil law rights conducted clearly in bad faith (abuse of right) are not allowed ….
> 2. In case of non-compliance with the requirements provided by Paragraph 1 of the present Article, a court, commercial court, or private arbitration tribunal, taking into account the nature and consequences of the abuse committed, may fully or partially deny the person protection of the right belonging to him and may also take other measures provided by statute …
> 4. If an abuse of right has entailed the violation of the right of another person, such person shall have the right to demand compensation for the harm caused by this.
> 5. The good faith of participants in civil-law relations and the reasonableness of their actions shall be presumed."

Article 10 is a somewhat special provision, which (based on general principles of good faith and reasonableness) allows the Russian court to impose civil liability without referring to a particular legal norm prohibiting the relevant type of conduct, in circumstances where the defendant has acted formally lawfully (i.e. where the defendant did not violate a specific legal rule or obligation). The legal prohibition of abuse of rights may operate both as a shield or a sword, i.e. it can afford a legal defence from another's abusive exercise of its civil rights, or it can serve as an element for a cause of action if another person inflicted damages by acts apparently lawful but which were exercised in an abusive manner.

Where a claimant seeks to rely on art.10, in addition to other elements of claim, the claimant must prove the following elements: (a) the abuser has exercised its own legal rights; (b) the exercise of those rights was for an abusive purpose; and (c) the misuse of rights was intentional.

Under Russian law a duty to act in good faith has been clarified by the Russian Supreme Court as follows:

> "When considering whether the parties acted in good or bad faith, it should be taken into account the behaviour expected from any participant to the civil-law commerce who takes into account the rights and legitimate interests of, and cooperates with, the other party, including by making available necessary information."[12]

This does not bring in a lot of clarity. However, it is clear that bad faith is a reverse side of good faith, that is, when a party to the civil-law relations acts contrary to the behaviour expected from it, dishonestly. It is obvious that the scope of application of the "good faith" principle and, accordingly, the notion of "bad faith" are quite vague. Therefore, civil law does not provide for a general sanction for all instances of conduct that is contrary to the good faith principle. The law specifies certain instances where bad faith conduct entails negative consequences for the wrongdoer. Abuse of rights is one such instance. Therefore, not all bad faith conduct (in the sense being not in good faith as opposed to an abuse of rights) is treated as an abuse of rights.

A claimant has a high burden of proof in relation to the above-mentioned elements of art.10 (i.e. abuse of rights). For instance, "exercise of rights for an abusive purpose" means that the "exercise of a right" was carried out with the purpose to misuse such right (i.e. to exercise a civil right under a rule of law in contradiction with the purpose for which it was introduced by this rule). In each case, whether there is such misuse would depend on the analysis of a particular right and having regard to the confines/limits of its proper exercise. In certain circumstances the fact that a person is exercising a right with direct intent to its own benefit would not make such exercise an abuse, unless, having regard to the purpose of the right based on the relevant rule, such exercise should be considered abusive. Moreover, abuse of rights is always an intentional act and reflects the mental attitude of the wrongdoer to its own acts, therefore only direct intent is of legal relevance (the wrongdoer must act with an abusive purpose).[13]

Therefore, it is that it is quite difficult to prove an abuse of right on the part of the defendant.

Authors' view on the discussed issues

Summary

Despite the fact that arts 10 and 1064 of the RCC are not *explicitly* limited in their scope of application, there are some *implied* limits, which are well recognised under Russian law being developed in the case law and reinforced in the doctrine. First, art.10 applies only in the exceptional situations. Second, art.1064 was originally devoted to the protection of absolute rights (*rights in rem*) only, rather than to the protection of relative rights (i.e. it was not designed to capture and compensate for such extravagant species as interference in other persons' contractual relations, pure economic loss or reflective losses).

[12] SC's Plenum Resolution No. 25 dated 23 June 2015.
[13] Note, however, that in civil law (particularly for legal entities) a different objective concept (in relation fault) applies instead of subjective element.

All in all, this means that the scope of application of arts 10 and 1064 in conjunction should be narrow.

Competition of claims and possible protection against tortious interference

First of all, we want to explain how Russian law works in cases involving arts 10 and 1064. As it will be seen from the cases discussed below, such cases mostly concern claims of major creditors against the persons controlling the actual debtors (or UBOs). In other words, claimants demand compensation not from the contractual debtor companies itself, but from the UBO directly. Also, in some cases, such UBOs are accused not only in mismanagement of the debtor companies, but also in interference in the commercial activity of a third person.

In issuing a tort claim under art.1064 the claimants also rely on art.10 in order to explain why an UBO should be liable for non-performance of a debt by its subsidiary or otherwise owned or controlled entity. As a general rule, such tort claim is unavailable under Russian law. This is a common approach that only a contractual debtor is liable for non-performance of a debt (i.e. not its shareholder or even an UBO). The rule that a claimant cannot bypass a contractual chain has been recognised in many cases in Russia.

Articles 308(3), 401 and 403 of the RCC serve as reference points why it is a counterparty who is responsible for non-performance of the obligation even if such non-performance was delegated to a third party or it was caused by a third person. It is no excuse that a third person's acts or inaction might have prevented performance.

Moreover, art.56 of the RCC enshrines the principle of separate corporate personality and separate liability of corporate entities. The founder (member) of a legal entity is not liable for obligations of the legal entity, and the legal entity is not liable for obligations of the founder (member).

Therefore, if a contractual relationship exists, then it is a contractual debtor who is liable for any losses caused to its counterparty by non-performance. The debtor cannot invoke acts of a third person as an excuse, whereas that third person cannot have a direct (non-contractual, tort-based) claim against the debtor's counterparty. The only way to allow such bypassing is for a creditor's claim against a non-party to fall within one of the exceptions identified below. Some of these exceptions concern only the notion of "interference" but do not apply in a situation where compensation is sought in respect of pure economic loss or reflective loss (which are unknown concepts under Russian law).

Exceptions to the general rule

The first exception to the general rule described above is joint and several liability of the parent company for the obligations of its subsidiary for transactions concluded by the latter in performance of instructions or with the consent of the parent company.[14]

The second exception is an insolvency exception.[15] Where the bankruptcy of a legal entity was caused by the founders (shareholders) or other controlling persons, secondary (subsidiary) liability may be established against such persons in the debtor's bankruptcy proceedings.

The third exception is a group of cases in which parties owing statutory duties in relation to goods have been held liable to the ultimate purchasers.[16]

There is also a possible fourth exception based on the concept of abuse of rights, which is a main theme in this article. It is controversial and it is not well established. It is difficult to define the precise scope of this exception, because some commentators argue that tort law cannot protect contractual rights at all and, also, due to a rather general nature of the prohibition of abuse of rights.

A claim against a third party (i.e. a controller of a contractual debtor (corporate entity)) is an extraordinary mechanism for protecting the violated rights of a company's creditors. Therefore, in our view, so that a claimant could avail of the fourth exception, it would be expected to have first pursued all available remedies against its contractual debtor itself, including by advancing its claim in insolvency proceedings if available. It would only be if all available possibilities to recover from the contractual debtor itself had been pursued and exhausted by the claimant, that it might be possible for an art.1064 claim to be brought by a claimant against a third party (which acts are said to have caused harm to the creditor's contractual rights) and for the claimant to establish loss caused by such third party.

Notion of harm

Initially, in the context of tortious liability, the notion of harm was narrowly construed, reflecting a recognised division in Russian law, between two categories of rights: absolute rights (or rights *in rem*) and relative rights (or rights in personam). The traditional view, developed in case law, was that art.1064 (as a general rule) only protected absolute rights.[17]

However, another approach has been developed in certain case law (in the context of "abuse of rights" cases) which supports a view that the notion of harm for the purposes of art.1064 should be understood more broadly. This case law is used by some authors to develop a position that it is possible under Russian law to compensate harm caused to relative rights.

[14] Article 67.3 of the RCC.
[15] Section III.2 of the Insolvency Law.
[16] See, e.g. Judgment of the Supreme Court (SC) dated 11 May 2018 in Case No. A57-15013/2016; Judgment of the SC dated 9 June 2016 in Case No. A41-5917/2015.
[17] See, e.g. Judgment of the Federal Commercial Court of the North-West Circuit dated 29 November 2005 in Case No. A26- 3330/2005-12.

Thus, two different views have been developed in the case law, leading to conflicting views about how far the relative rights are protected. The apparent conflict is reconciled by accepting that in general art.1064 only protects absolute rights, but that, as explained above, relative rights (including contractual rights) may also be protected in cases falling within certain narrow exceptions.

Article 1064 requires harm to the person or property. Where the property is said to be a contractual right (i.e. some economic interest in performing of the obligation by the counterparty), it must be that right that is harmed. It is not enough that the claimant has not been paid or has suffered some other loss: the contractual right to payment must itself have been harmed in order to establish the necessary harm to property. We believe that a Russian court would consider this only to be established where (a) prior to the allegedly wrongful act of a tortfeasor the contractual debtor had the means to discharge its contractual obligation (e.g. money or other assets with which to pay a debt) and it can be shown that it would have discharged that obligation, but (b) the defendant's allegedly wrongful act permanently deprives the contractual creditor of the means to obtain payment of the contractual obligation from its contractual debtor.

Therefore, when establishing harm to a contractual right for the purposes of an art.1064 claim, a Russian court would consider that harm can only be said to have been caused by the acts of a non-party to the contract where those acts have caused the contractual creditor to have a complete and permanent inability to receive performance from the contractual debtor, but not in the case of a mere ongoing delay in the debtor's performance of such obligation, or where the contractual debtor remains solvent, or where the creditor has or had other means to pursue performance against the assets of the contractual debtor. It would have to be an exceptional case where the creditor can show it had no other possibility to receive payment under the contract from the contractual debtor. It is perhaps this special factor which could allow a Russian court to ignore the principle of competition of claims and other principles mentioned above, and to allow the claimant to resort to a claim against a non-party to a contract.

Now with all these principles in mind, we invite a reader to look at them through the English cases in which they were considered. The analysis of the cases is set out in part 2 of this article to be published in the next issue of the journal.