

Update on JKX vs. Ukraine “Saga”

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The Ukrainian “saga” on the enforcement of the SCC emergency arbitrator’s award continues, as the case is pending the second round of cassation review.

Arbitration proceedings were initiated by Dutch and English investors Oil&Gas PLC and Poltava Gas B.V. (JKX or Claimants) on 7 January 2015. The case concerns the alleged Ukraine’s failure to comply with its obligations under the Energy Charter Treaty, the *UK-Ukraine BIT* (1993), and the *Netherlands-Ukraine BIT* (1994). On 28 December 2014 Ukraine enacted the *Act of Ukraine on Tax Reform Amendments to the Tax Code of Ukraine and Other Legislative Acts*. This Act provides for an increase in royalty payments on gas production from the previously applicable 28% to 55%. According to JKX, these provisions conflict with Ukraine’s obligations to ensure fair and equitable treatment of investments. JKX claims it has suffered losses resulting from these violations and demands compensation in the amount of USD 270 million.

Emergency arbitrator proceedings in Stockholm

The Claimants requested the appointment of emergency arbitrator in accordance with the SCC Arbitration Rules. On 8 January 2015 the parties were informed of the appointment of an emergency arbitrator and that the seat of arbitration will be Stockholm.

On 12 January 2015 the parties were told that the request of the emergency arbitrator to extend the period for the consideration of the application had been accepted by the SCC. Ukraine submitted a written confirmation that the Ministry

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of Justice had received the notice on the appointment of the emergency arbitrator. However, in the end, Ukraine did not participate in these proceedings.

On 14 January 2015 the emergency arbitrator rendered an award ordering Ukraine to refrain from collecting gas production royalties from JKX at the rate exceeding the previously applicable 28% fee.

Problems with enforcing an emergency arbitrator’s award in Ukraine

JKX filed a motion for recognition and enforcement of the emergency arbitrator’s award in Ukraine. The government of Ukraine argued that the decision of the emergency arbitrator was not enforceable, based on the following:

1. Ukraine was not properly notified about the emergency arbitration proceedings,
2. the Claimant failed to comply with the three-month cooling-off period,
3. referral of the case to an emergency arbitrator had fallen outside the party’s agreement to arbitrate, and
4. enforcement of the emergency arbitrator’s award would violate Ukrainian public policy.

The Pechersky District Court of Kiev granted the motion for enforcement on 8 June 2015 rejecting all objections raised by Ukraine. The court disregarded the argument on cooling-off period. The court found that notification through emails should qualify as a proper notification, and held that the award was rendered within the scope of the arbitration agreement, as the appointment of emergency arbitrator was provided for by the applicable arbitration

rules. The court further stated that the award did not violate Ukrainian public policy, as it did not change the existing hydrocarbon production royalty system of Ukraine.

The Ukrainian Ministry of Justice filed an appeal to the Kiev City Court of Appeal relying on the same arguments as before the court of first instance. However, the Court of Appeal took into consideration only the argument regarding the violation of public policy. The court stated that the relations concerning taxes and fees are regulated by the *Tax Code of Ukraine*. In the court’s view, since the tax rate is a matter governed exclusively by the *Tax Code*, the enforcement of the award would violate the fundamental principles of taxation and would, therefore, violate the public policy of Ukraine. The court also highlighted the losses that the Ukrainian budget would incur as a result of changing the established tax rates. The Court of Appeal reversed the decision of the Pechersky District Court of Kiev City and refused the recognition and enforcement of emergency arbitrator’s award on 17 September 2015.

JKX continues fighting for enforcement of the emergency arbitrator’s award

JKX filed a cassation appeal before the High Specialized Court of Ukraine for Civil and Criminal Cases. The High Specialized Court remitted the case to the Kiev City Court of Appeal on 24 February 2016. It held that the Court of Appeal failed to consider that the award does not change the scope of rights and obligations of the parties, but only temporarily obliges Ukraine to refrain from imposing a royalty on gas production exceeding 28%.

On 17 May 2016 the Kiev City Court of Appeal upheld the decision of the Pechersky District Court of Kiev City by granting the motion for enforcement, and dismissing the appeal of the Ministry of Justice (Ministry).

The Kiev City Court of Appeal held that the award does not change the scope of the rights and obligations of the parties to the dispute but, rather, it temporarily obliges Ukraine to refrain from imposing gas production royalty exceeding 28%. Furthermore, the court established that the award neither changes the taxation system of Ukraine, nor replaces the provisions of the *Tax Code of Ukraine*. The decision of the Kiev City Court of Appeal provides for an adequate reasoning with respect to public policy and the proper notification of a party. In that regard, the court construed the notion of public policy to encompass “the state’s legal order, the defining principles and basic elements that form the fundamentals

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of the state’s independence, integrity, self-sustainability and inviolability, fundamental constitutional rights, freedoms, guarantees etc.”. The court further elaborated on the Ministry’s failure to demonstrate an actual infringement of public policy of Ukraine, i.e. the change in the taxation system in Ukraine, which would take place when the award would be enforced. The court added that the award did not affect general rates and conditions of rental payments.

The latest developments

The Ministry of Justice filed a cassation appeal against the decision adopted by the Kiev City Court of Appeal of 17 May 2016. On 29 June 2016 the High Specialized Court of Ukraine for Civil and Criminal Cases decided to commence another round of the judicial review. Pursuant to the *Civil Procedure Code of Ukraine* decision and resolution of the cassation court come into ef-

fect upon their announcement. Furthermore, upon the announcement of the relevant cassation court decision, the reversed decisions and resolutions of the first instance court or the appeal instance court lose their force. It is important to note that in some exceptional circumstances cases may be reviewed by the Supreme Court of Ukraine.

The case is pending another cassation review and the future decision of the High Specialized Court is expected to be a probe of the enforceability of the awards of emergency arbitrators in Ukraine, and at this moment it is difficult to predict when the Ukrainian “saga” on the enforcement of emergency arbitrator’s award will end.

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