

The VimpelCom Case

Overview of court practice on termination of leases

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The VimpelCom Case

The VimpelCom Case (1)

The tenant (PAO Vimpel-Communications) got the court to set a “currency band” in a long-term lease agreement for office premises (Case No.A40-83845/15-54-532)

- VimpelCom’s position:
 - There was a considerable **increase in the RUB/USD exchange rate**
 - The Bank of Russia refused **to introduce a currency band and currency interventions**
 - **Economic sanctions** were imposed on Russia→ material change of circumstances (Art. 451 of the Civil Code)
- **The first instance court** refused to terminate the agreement in line with the established court practice on material change of circumstances, **BUT** nonetheless granted VimpelCom’s prayer for judicial modification by setting a “currency band”

The VimpelCom Case (2)

- The court refused to terminate the lease agreement:
 - The **change in the exchange rate** does not constitute an unforeseeable circumstance
 - The **change in monetary or currency policy of the Bank of Russia** similarly does not constitute a material change of circumstances (the court did not comment on the argument regarding imposition of economic sanctions)
 - denominating payment obligations in a foreign currency implies a risk of change in exchange rates, which VimpelCom assumed **as a business risk**
- The court's reasoning for setting a currency band:
 - No one has the right to gain an advantage from their **own misconduct**
 - The amount of **rent** should not exceed **typical rates** paid for leasing similar premises and substantially exceeding the market price for rent could entail **unjust enrichment** for a landlord
 - **In order to maintain a balance between the parties' material interests**, the court has decided to judicially modify the lease agreement, instituting a currency band for calculating the ruble equivalent of the rent
 - The court has therefore established limits on the RUB/USD exchange rate on the basis of **VimpelCom's suggestions** (in the absence of any competing suggestions from Tizpribor)

The VimpelCom Case (3)

On March 28, 2016 **the appellate court** reversed the decision of the court of first instance:

- Guided *by the principle of freedom of contract*, **the parties agreed to the procedure for setting and changing rent**, which does not provide for change at one party's request
- *Insistence on performance* by the parties of the agreed terms of the contract **is not an abuse of right**
- The agreement *was not terminated*, so the landlord **could not have had unjust enrichment**

The court reversed the decision of the court of first instance and rejected VimpelCom's claim to introduce a currency band

After the VimpelCom Case: is there still a risk for foreign-currency-denominated contracts?

- **Court practice**

The reversal of the decision on the VimpelCom case in the appellate court **has upheld the established practice of the commercial courts of rejecting** such claims

- **Initiatives to introduce a mandatory ban**

Back in August of 2015 the Ministry of Industry and Trade proposed including in the RF Civil Code a ban on setting rent in foreign currency in lease agreements

- **The draft law has not yet been published in open sources**

- The idea of imperative regulation is ambiguous:

- Not in line with *freedom of contract* principles
- Risk of evading the new restrictions: the rent amount does not have to be denominated in foreign currency – *e.g. foreign currency pegging can be achieved by using an adjustment factor*

Overview of current court practice on the termination of lease agreements

What is the basis for the conclusions we want to share?

- Overview of the most pressing issues of terminating lease agreements: is it possible to withdraw from a contract that *is being performed by the parties* but is commercially disadvantageous?
- Practice trends in crisis conditions: overview of court practice on certain matters since 2009
- Thinking ahead: how will the changes to the Civil Code that came into effect in June 2015 affect termination of lease agreements?

Lack of state registration

- Lack of registration of a lease agreement for a term of at least a year:

Does not work after the Supreme Commercial Court clarifications in 2013:

“14. If the owner has transferred the property for use, and the other party has accepted it without any comment, agreement on the amount of the fee for use of the property and other terms of use was reached by the parties and performed by them, then <...> it has bound them with an obligation that cannot be arbitrarily modified by one of the parties (Art.310 of the Civil Code) and there are no grounds for the court to apply the provisions of articles 1102 and 1105 of the Civil Code [unjust enrichment]”

RF Supreme Commercial Court Plenum Ruling No. 73 of November 17, 2011
(version of January 25, 2013)

*“As soon as the relevant ground for state registration of the right arises, the parties to such transaction ... **may not in their relationship** refer in bad faith to lack of a record of that right in the state register”*

RF Supreme Court Plenum Ruling No. 25 of June 25, 2015

Material change of circumstances

The courts do not recognize increase in the exchange rate of the currency in which the rent is denominated as a material change of circumstances

<...> inflation processes are not unforeseeable circumstances. <...> When entering into contractual relations the parties should have predicted the economic situation, so they could not rule out the likelihood of a price increase while the transaction was being performed.

RF Supreme Commercial Court Presidium Ruling No. 1074/10 of April 13, 2010 on case No. A40-90259/08-28-767

Also:

- Increase in operating costs
 - Deterioration of financial circumstances and economic activity
 - Staff downsizing
 - Decreased demand for product sold
 - Cessation of activity in the premises (tenant's departure)
 - Institution of bankruptcy proceedings
- are not considered a material change of circumstances

Lease as a contract of accession (1)

*In cases where <...> when entering into a contract the draft of which was proposed by one of the parties and it contained terms that were clearly onerous for the counterparty and materially violating the balance of the parties' interests (**unfair contractual terms**), and the counterparty was placed in a position making it difficult for them to negotiate other contents of certain terms of the contract (in other words, it was the **weak party to the contract**), **the court may apply to such contract the provisions on contracts of accession by modifying or terminating the relevant contract at the request of such counterparty.***

P. 9 of RF SCC Plenum Ruling No.16 “On Freedom of Contract and its Limits” of March 14, 2014

- When interpreting **unfair contractual terms** the court must evaluate:
 - The actual negotiation positions of the parties
 - Whether the party was economically “forced” to accede to the suggested terms
 - The degree of professionalism
 - Competition on the market
 - Whether the adhering party had the ability to negotiate and enter into a similar contract with third parties

P. 10 of RF SCC Plenum Ruling “On Freedom of Contract and its Limits”

Lease as a contract of accession (2)

- Since June 2015 the Civil Code (Art. 428) has explicitly stated that it is possible to **terminate a contract as a contract of accession, if the negotiating abilities of the parties are clearly unequal**
 - The terms of the contract were determined by one of the parties
 - The other party was placed in a position making it **substantially** difficult to negotiate alternative terms of the contract due to **clearly** unequal bargaining power
- There are **several court decisions** where **the courts granted tenants' claims to terminate lease agreements** citing the RF SCC Plenum Ruling “On Freedom of Contract” and Article 428 of the Civil Code
 - *tenants → individuals (individual entrepreneurs)*
 - *regional (including appellate) courts*

Lease as a contract of accession (3)

Recommendations for the “powerful” party:

- Written confirmation *of negotiations held* with the weak party (correspondence, minutes of meetings, etc.)
- When refusing to agree to terms suggested by the weak party, *to provide a written and reasoned justification of its position*, and also where possible to suggest alternative solutions
- To state in the contract that
 - The terms *are not clearly onerous* for the parties, and signing the contract does not result in a *material violation of the balance of interests* of the parties
 - Signing the contract *is not coercion for the weak party*, and it had opportunities to negotiate and sign a similar contract with third parties
 - Both parties possess *the necessary degree of professionalism*, and they had the opportunity to seek legal assistance

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Thank you

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