THE PROBLEM OF CHOOSING THE LAW APPLICABLE TO ARBITRATION PROCEEDINGS AND ARBITRATION AGREEMENT FROM THE KAZAKH LEGISLATION PERSPECTIVE

Valikhan Shaikenov
AEQUITAS Law Firm, Partner and Head of Dispute Resolution
e-mail: v.shaikenov@aequitas.kz

Ardak Idayatova
AEQUITAS Law Firm, Senior Associate, Dispute Resolution
e-mail: a.idayatova@aequitas.kz

The problems of court practice [1, 2, 3] and statutory regulation [4, 5, 6] largely complicate arbitration proceedings in the Republic of Kazakhstan (hereinafter, the RK). This is why, if the situation so allows, the parties prefer to settle disputes in arbitration-friendly countries.[1]

The choice of the seat of arbitration is not logistical at all. In countries fostering arbitration development, the courts[2] and legislation[3] normally regard the choice of the seat of arbitration as the choice of law applicable to the arbitration proceedings (although, of course, the law applicable to arbitration proceedings must not always coincide with the chosen seat of arbitration [7]). Thus, in the practice of a number of countries, the choice of the seat of arbitration has a legal implication. Terminologically, the legal place of arbitration proceedings (seat of arbitration) is opposed to the physical place of arbitration hearings (venue of arbitration).

In those countries, the choice of the seat of arbitration means resolving the *conflict-of-laws* issue regarding the law applicable to the arbitration proceedings. The issue of the choice of law applicable to the arbitration agreement must be resolved independently [8].

Posing the Conflict-of-Laws Issue

When choosing a foreign seat of arbitration, the parties strive to prevent application of Kazakh law to their arbitration proceedings. Besides, the parties often assume that choosing, for example, London, as a seat of arbitration means that the arbitration clause will be governed by the law of England as well.

Even if obvious from the English law standpoint, the correctness of this assumption does not indubitably follow from the Kazakh legislation: neither from the RK Law on Arbitration of 8 April 2016 (hereinafter, the Arbitration Law), nor from the RK Civil Code (hereinafter, the Civil Code) or from the RK Civil Procedure Code of 31 October 2015 ((hereinafter, the CPC).

Internal contradictions of the Kazakh legislation, inconsistent court practice and significant deviations from the common standards of commercial arbitration formed in the developed world may lead to the situation where the parties' choosing a foreign seat of arbitration would not mean to a Kazakh court that they have chosen a foreign law as applicable to the foreign proceedings. This, in turn, makes it possible for the Kazakh court to apply Kazakh law to the arbitration proceedings and arbitration agreement.

As a separate consequence, it may be difficult or impossible at all to enforce the foreign arbitral award rendered in contradiction to the Kazakhstan statutory requirements governing arbitration (although the

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[1] According to the poll conducted in 2015 by the Queen Mary University of London (QUML) in conjunction with White & Case law firm, the top popular seats of arbitration are London, Paris, Hong Kong, Singapore, Geneva, New York and Stockholm. URL: http://www.arbitration.qmul.ac.uk/docs/164761.pdf.

[2] *RosInvestCo UK Ltd. v. The Russian Federation*, Judgment of the Supreme Court of Sweden, 12 November 2010, Case No. Ö 2301-09/NJA 2010, s. 508 ("The choice of the applicable procedural law normally results from the selection of the place (the seat) of the arbitration").

[3] See, for instance, Article 3 of the 1996 UK Arbitration Act; Article 47 of the 1996 Sweden Arbitration Law.

parties thought that the Kazakh legislation should not apply to their arbitrated dispute, arbitration clause and the rendered award).

The preamble to the Arbitration Law defines its spatial scope of application. While this provision allows for excluding application of this law in certain cases (we will expand on this further below), it does not solve the primary issue – that of the *conflict-of-laws*, namely, the issue of choosing the law applicable to the arbitration proceedings and arbitration agreement. This acquires a particular significance in the light of the CPC's "attempts" to regulate some relations stemming from the arbitration agreement (we will also expand on this further below).

Pursuant to the Arbitration Law preamble, the Law "shall govern social relations arising *in the process of arbitration activities in the territory of the Republic of Kazakhstan*, and the procedure and conditions for the recognition and enforcement of arbitral awards in Kazakhstan."

Here, the "arbitration" means "an arbitration specifically formed to review a particular dispute, or a permanent arbitration." The conceptual error in the definition of the concept of "arbitration" has already been discussed in literature [4]. As a result of that error, the "arbitration," instead of meaning the dispute settlement method and dispute review procedure itself, means two at a time functionally different concepts: (i) the arbitration institution whose functions should include only assistance in the dispute administration; and (ii) the arbitral tribunal reviewing the dispute.

Thus, the literal reading of the Arbitration Law preamble may call for two possible interpretations (without regard to the recognition and enforcement of arbitral awards in Kazakhstan):

1) The Arbitration Law applies to relations arising in the process of an arbitration institution's activities in the territory of Kazakhstan; and
2) The Arbitration Law applies to relations arising in the process of an arbitral tribunal's activities in the territory of Kazakhstan.

If adhering to the second interpretation based on the error made in the definition of the "arbitration" concept, then, absent a doctrinal interpretation, the existing language may mean application of the Arbitration Law to the work of an arbitral tribunal actually seated in Kazakhstan.

However, the problem is nested deeper – deeper than merely deciding on the Arbitration Law's applicability or inapplicability to arbitration proceedings or arbitration agreement [9]. The problem is of a conflict-of-laws nature and is in the applicability to the arbitration proceedings and arbitration agreement of the *law and order of a particular country in general*.

The Arbitration Law could help in the resolution of that conflict-of-laws problem, had it specified that the reference to the seat of arbitration means the choice of the country whose law applies to the arbitration proceedings and arbitration agreement. However, the conflict-of-laws issue cannot and must not always be resolved in a law governing the arbitration activities in a given country (at least due to the fact that, as a rule, the arbitration law applies to arbitration proceedings taking place in the relevant country, i. e., using such proceedings is a consequence of the already made conflict-of-laws choice).

For instance, the UNCITRAL Model Law[4], coming in line with which was declared as one of the objectives of adopting the Arbitration Law[5], also does not resolve the conflict-of-laws issue, but only the issue of applying a certain given law to arbitration proceedings.

Article 1 ("Scope of Application") of the Model Law says that the national law on arbitration is to apply only "if the **place** of arbitration is in the territory of this State" (except for some provisions applicable for foreign arbitrations as to injunctive measures, enforcement of foreign arbitral awards, etc.). However, Article 20.1 of the Model Law never answers the conflict question of the law applicable to the arbitration

[4] UNCITRAL 1985 Model Law on International Commercial Arbitration (as amended in 2006). URL: http://www.uncitral.org/pdf/russian/texts/arbitration/ml-arb/07-87000_Ebook.pdf.

[5] See Concept of the Draft Law of the Republic of Kazakhstan "On Commercial Arbitration," Ref. No. 8-3-340 of 13 November 2014.

proceedings and arbitration agreement, just establishing that the "parties are free to agree on the place of arbitration. Failing such agreement, the place of arbitration shall be determined by the arbitral tribunal having regard to the circumstances of the case, including the convenience of the parties."[6]

Resolving the Conflict-of-Laws Issue in Arbitration-Friendly Countries

Most Contracting States to the New York Convention[7] treat the choice of the seat of arbitration as a legal concept (not just the geographical choice of the place of hearings). This concept is essentially in that the parties, when choosing the seat of arbitration and specifying it in the arbitration clause, are thus agreeing on the *lex loci arbitri* – law applicable to the arbitration proceedings. If the parties have specified London as the seat of arbitration, their arbitration – according to the widespread interpretation of the New York Convention – will be subjected to the England's national law on arbitration.

This principle was originally worded in the 1923 Geneva Protocol on Arbitration Clauses[8], its Article 2 saying that the "arbitral procedure, including the constitution of the arbitral tribunal, shall be governed by the will of the parties and by the *law of the country in whose territory the arbitration takes place*." Despite all the shortcomings of the Geneva Protocol[9], the New York and the European[10] Conventions adopted thereafter no longer contained the so expressly worded conflict-of-laws rule of the choice of law applicable to arbitration proceedings.

Still, the state courts of the Contracting States to the New York Convention have drawn a similar rule by broadly interpreting the rule of subparagraphs "a" and "d" of paragraph 1 of Article V of the Convention, which had obviously not been intended to resolve the conflict-of-laws issue.

> "1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:
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> (a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, *failing any indication thereon, under the law of the country where the award was made; or*
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> (d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was *not in accordance with the law of the country where the arbitration took place*…" [10, 11].

The European Convention, without conflicting with the New York Convention, set out in its paragraph 2 of Article VI an even more clear-cut rule:

> "In taking a decision concerning the existence or the validity of an arbitration agreement, courts of Contracting States shall examine the validity of such agreement with reference to the capacity of the parties, under the law applicable to them, and with reference to other questions:
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> (a) under the law to which the parties have subjected their arbitration agreement;

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[6] The Explanatory Note by the UNCITRAL Secretariat on the 1985 Model Law on International Commercial Arbitration (as amended in 2006) shows that the drafters did not pursue an objective to recommend any particular method to resolve the conflict-of-law issue, supposing that each sovereign decides on this issue on its own: "In most legal systems, the place of arbitration is the exclusive criterion for determining the applicability of national law and, where the national law allows parties to choose the procedural law of a State other than that where the arbitration takes place, experience shows that parties rarely make use of that possibility."

[7] Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 10 June 1958).

[8] Protocol on Arbitration Clauses signed in Geneva on 24 September 1923.

[9] Together with the 1927 Geneva Convention on the Recognition and Enforcement of Foreign Arbitral Awards losing force in connection with the adoption of the 1958 New York Convention.

[10] European Convention on International Commercial Arbitration (Geneva, 21 April 1961).

(b) failing any indication thereon, *under the law of the country in which the award is to be made*;

(c) failing any indication as to the law to which the parties have subjected the agreement, and where at the time when the question is raised in court the country in which the award is to be made cannot be determined, under the competent *law by virtue of the rules of conflict of the court seized of the dispute*."

Some courts have been deducing the conflict-of-laws rule *lex arbitri* from the similar rules contained in the arbitration laws of their countries borrowed from Articles 34(2)(a)(i) and 36(1)(a)(i) of the UNCITRAL Model Law [10].

Why Such Solution to the Conflict-of-Laws Issue is Inacceptable in Kazakhstan

The Kazakh courts could also follow that way, but for the impediments stemming from the Arbitration Law, the CPC and the status of the New York and European Conventions described below.

Kazakhstan acceded to the New York[11] and the European[12] Conventions via the RK President Edicts not having the force of law[13]. Therefore, these Conventions, although constituting a part of the RK effective legislation, do not have the status of ratified international treaties, hence, do not prevail over the RK laws[14].

At the same time, Article 57.1.1 of the Arbitration Law and Article 255.1.1 of the CPC contain the rules governing, same as Article V of the New York Convention, the grounds for refusing the recognition and enforcement of an arbitral award. However, while the New York and the European Conventions allow (absent the choice of law applicable to the arbitration agreement) for evaluating the existence and validity of the arbitration agreement under the law of the country where the award has been made, the said rules of the Arbitration Law and the CPC in a similar situation allow the Kazakh court to refuse recognition of a foreign arbitral award, if the arbitration agreement is invalid *under the laws of the Republic of Kazakhstan*.

Given that the Arbitration Law and the CPC prevail over the New York and the European Conventions, even if Kazakh courts deduce the conflict-of-laws rule from the rules for the recognition and enforcement of arbitral awards, they will have to rely of Article 57.1.1 of the Arbitration Law and Article 255.1.1 of the CPC, not on the Conventions. This, in turn, should drive the courts to apply the law of the Republic of Kazakhstan (i. e., *lex fori*) to the arbitration agreements in which the parties failed to specify the applicable law, even if the parties had stated in the arbitration agreement a foreign seat of arbitration, and, according to such choice of the parties, the arbitration had already been formed under the foreign law and had rendered an award.

Such interpretation would entail an obvious violation of the parties' will and would deprive the winning party of what it would have been entitled to count on when entering into the arbitration agreement; leave

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[11] Edict No. 2485 of the President of the Republic of Kazakhstan "On Accession of the Republic of Kazakhstan to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards" dated 4 October 1995.

[12] Edict No. 2484 of the President of the Republic of Kazakhstan "On Accession of the Republic of Kazakhstan to the 1961 European Convention on International Commercial Arbitration" dated 4 October 1995.

[13] As at the time of those edicts adoption, due to absence of the supreme representative authority, in effect was the RK Law "On Temporary Delegation of Additional Powers to the President of the Republic of Kazakhstan and Heads of Local Administrations" dated 10 December 1993, entitling the President to adopt edicts having the force of law and, in particular, to ratify and denounce international treaties. Some Kazakh lawyers voiced an opinion that presidential edicts on accession to the New York and European conventions should be construed as edicts having the force of law, since the RK President, as a representative of the executive branch of power, had no powers to have the Republic access the international treaties. We deem this conclusion erroneous, because the RK President, by virtue of the RK 1995 Constitution (paragraph 11 of Article 44) and the Vienna Convention on the Law of Treaties of 23 May 1969 (subparagraph a) of paragraph 2 of Article 7), was empowered to represent the state in international relations and enter on behalf of the Republic into international treaties in his status of the head of state, not just as a person temporarily exercising the functions of the supreme representative authority. Therefore, having adopted the edict not having the force of law the President had evidently exercised his power of the head of state, not the supreme representative authority.

[14] Article 4.3 of the Constitution of the Republic of Kazakhstan.

alone that applying to the arbitration agreement the national law of the country of the court (*lex fori*), not the *lex arbitri*, differs in principle with the standards of international commercial arbitration commonly accepted in the developed world.

Possible Solution to the Conflict-of-Laws Issue from the Kazakh Law Perspective

Given the current regulation of arbitration (which undoubtedly needs a radical reform), it looks like the only reasonable solution to the conflict-of-laws issue would be to refrain from using Article 57 of the Arbitration law and Article 255 of the CPC to deduce the conflict-of-laws rule. This is maintained by very strong arguments.

The logics used by the courts abroad in order to deduce the conflict-of-laws rule from Article V of the New York Convention is not flawless, taking into account that this rule is of an exclusively procedural nature (establishes the grounds for refusing to issue the writ of execution/enforcement order) and does not regulate the substantive law relations (in particular, validity of arbitration agreement, lawfulness of arbitration proceedings, etc.).

Still, it one proceeds from the civil nature of arbitration, it would be reasonable to resolve the conflict-of-laws issue regarding the law applicable to the arbitration proceedings or arbitration agreement in the section of the Civil Code dedicated to private international law. For example, this was the way the French courts have taken [8].

Article 1113 of the Civil Code offers the rules for determining the law applicable to a contract in case there is no agreement of the parties. Since the arbitration agreement qualifies as none of the contracts listed in paragraphs 1–3 of Article 1113 of the Civil Code and since performance of the arbitration agreement not by one, but by all parties thereto "has a decisive meaning for the content … of the contract" (paragraph 4), it would be reasonable to apply to the arbitration agreement the law of the country with which the contract *is most closely connected*, as proposed in Article 1113.4 of the Civil Code. The reference to the seat of arbitration may well be regarded as a sufficient conflict-of-laws peg for determining the closest connection with the law of the relevant country. In other words, relying on Article 1113.4 of the Civil Code, a conclusion is possible that the parties, having specified the seat of arbitration, have made a conflict-of-laws choice in favor of the country where the arbitration is to take place.

Hence, there is no need to use Article 255 of the CPC in order to deduce the conflict-of-laws rule, because the conflict may be resolved by the civil law methods, including private international law and arbitration agreement itself. If it were impossible to find the conflict resolution in civil law, as an ultimate measure, it would be necessary to resort to Article 57 of the Arbitration Law and Article 255 of the CPC.

Implications of the Conflict-of-Laws Issue Resolution

Resolution of the conflict-of-laws problem in respect of the law applicable to the arbitration proceedings and arbitration agreement further permits us to analyze each questionable rule of the Kazakh legislation as to its applicability to relations stemming from the arbitration dispute. Let us consider some practically significant examples.

Refusal to Issue Enforcement Order Because of Arbitration Procedure Violation

Pursuant to Article 255.1 of the CPC, the court passes a ruling to refuse issuance of enforcement order to enforce an arbitral award, if the party against which the award has been rendered provides to the court evidences that the arbitration composition or the arbitration procedure has not been in compliance with the requirements of the *law*.

Until the conflict-of-laws issue was resolved, it would have been unclear which law was meant. Specifying the seat of arbitration in the arbitration clause enables us to apply *lex arbitri* to the arbitration procedure. This means that if arbitrating a dispute abroad, the party against which the arbitral award is rendered will have no right to refer to non-compliance of the arbitration procedure to the Kazakh legislation in accordance with the procedure established by Article 255.1 of the CPC.

The same position should also be maintained in respect of refusal to recognize a foreign arbitral award on the grounds that the arbitration agreement does not comply with the RK law. As substantiated above, only the limiting interpretation of Article 255.1 of the CPC allows, given the current regulation, to ensure the legitimate interests of the parties to arbitration clause and attain a legal result.

Scope of Application of the Arbitration Law

Preamble to the Arbitration Law gives no clear notion of it scope of application. What should be understood as the "arbitration activities in the RK territory"? Does this mean arbitration proceedings subjected to Kazakh law? Or an arbitration agreement governed by the RK law? Or a physical place of arbitration hearings? Let us look at some examples where the answers to the above questions are meaningful for the resolution of the Arbitration Law applicability issue.

Permitting Procedure for Certain Categories of Entities to Execute Arbitration Clauses

For example, Article 8.10 of the Arbitration Law establishes a permitting procedure for arbitration agreement execution by governmental agencies, state enterprises and legal entities in which fifty or more percent of voting shares (participation interests in the charter capital) are state-owned, directly or indirectly. In other words, the Article limits the civil legal capacity of legal entities.

If one assumes that the arbitration agreement is governed by foreign law, does this mean that the enumerated entities may freely enter into arbitration agreements? The answer to this question should most likely be "no," taking into account the stringent conflict-of-laws pegging of legal entity's civil legal capacity: it is determined by the law of the country in which the legal entity has been organized (Articles 1100 and 1101.1 of the Civil Code). The legislator hardly meant to establish the permitting procedure for entering into arbitration agreements only for those instances where arbitration proceedings and arbitration agreements are governed by the law of Kazakhstan. The permitting procedure was most probably intended for all instances where the competence of state courts is excluded, and this occurs irrespective of which law the arbitration agreement is governed by.

Arbitrability of Disputes

Article 8.8 of the Arbitration Law defines as non-arbitrable certain categories of disputes (e. g., those touching upon the interests of minors, disputes in rehabilitation or bankruptcy, disputes between natural monopoly entities and their consumers, etc.).

In the court practice of foreign states, they deduce from Article V.2.(a) of the New York Convention a stern conflict-of-laws pegging "according to which, when deciding on the recognition and enforcement of a foreign arbitral award, the issue of the dispute subject matter arbitrability is always subjected to *lex fori* (the national law of the country of the court) and does not depend on *lex arbitri* to which the arbitration clause may be subjected" [12]. Following this logics, a Kazakh court may refuse issuance of an enforcement order for a foreign arbitral award due to the dispute's non-arbitrability from the Kazakh law perspective, although the arbitration proceedings and the arbitration agreement are governed by foreign law. All the more that this ground is also stipulated by Article 255.1.1 of the CPC.

Unilateral Withdrawal from Arbitration Agreement

Although paragraph 5 of Article 9 dealing with unilateral withdrawal has been deleted from the Arbitration Law[15], it remains relevant to instances where one of the parties has attempted to withdraw from the arbitration clause in the period when this rule was still in effect. In this case, the issue is easily resolvable: if the arbitration agreement is governed by foreign law, this rule is not to apply, because the

[15] RK Law No. 49-VI "On Introduction of Amendments into Certain Legislative Acts of the Republic of Kazakhstan on the Issues of Improvement of Civil and Banking Legislation and Improvement of Conditions for Entrepreneurial Activities" dated 27 February 2017.

law applicable to a contract covers, by virtue of Article 1115.1.5 of the Civil Code, the contract termination.

The above examples demonstrate the need to resolve the issue of choosing the law applicable to the arbitration agreement and arbitration procedure. And even if the reader does not agree with the ways to resolve particular "conflicts" proposed by the authors, we believe that the posing of the conflict-of-laws problem should in itself be of practical and theoretical value.

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