

# CROSS-BORDER AND DOMESTIC LEGAL CHALLENGES

Article



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## Application and Renunciation of English Contract Law in Russia in Light of Recent Developments in the Social and Economic Environment

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**Abstract:** The paper outlines the prospects and problems surrounding the application of English contract law in Russia in light of the recent development in the social economic environment in Russia. This development has been predominantly influenced by the beginning of the Special Military Operation (the SMO) in February 2022 and by the Western sanction policy that was implemented thereafter. Since the collapse of the Soviet Union in 1991, Russian contract law has been significantly reformed. This has been achieved by the introduction of the principle of freedom of contract and autonomy of will into the Russian legal system in an explicit and detailed manner. As a result, parties to international contracts have widely used the right to choose any national law as applicable to their arrangements. For decades, it has been a common business practice in Russia to subject international contracts, specifically financial deals as well as mergers and acquisition transactions, to English law. This happened because of the unique instruments of English law which did not have any equivalent in Russian law. Due to the high demand for these instruments from the business community, certain amendments were introduced in the Russian Civil Code in 2015.

These amendments implemented some contract law instruments which have their origin in English law. Consequently, Russian contract law has become more business oriented. Many international contracts concluded before February 2022, and some contracts concluded thereafter are still regulated by English law. Russian judicial practice proves that application of English law to contracts does not entail application of foreign sanctions and Russian counter-sanctions to the respective contractual relations. These sanctions and counter-measures are not regarded as a part of contract law applicable to contracts. Furthermore, English contract law allows aggrieved parties to successfully protect their interests in cases where their counterparts committed a breach of contract as a result of voluntarily following the sanction policy.

Keywords: credit agreements; conditions precedent; warranties; representations; covenants; remedies; compensation; damages; sanctions; penalty; liability; breach; frustration; common law; indemnity

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## Contents

I. Introduction .....	929
II. Russian Practice of Application of English Contract Law .....	930
II.1. Instruments of English Contract Law .....	930
II.2. Remedies for Breach of Contract under English Law .....	933
III. Failure to Fulfil Contractual Obligations and Sanctions .....	937
III.1. Principle of Strict Liability .....	937
III.2. Doctrine of Frustration and Sanctions .....	938
IV. Influence of English Law on Russian Contract Law .....	943
V. The Prospects of Using English Law by Russian Courts .....	946
VI. Conclusion .....	948
References .....	948

## I. Introduction

Until the beginning of the Special Military Operation (SMO) in February 2022, English law was one of the most widely used national legal systems in transactions between Russian and foreign parties. Over

80 % of mergers and acquisition transactions (M&A) were governed by English law (Ivory and Rogoza, 2012, p. 5). The popularity of English law can be explained by such factors as the presence of legal instruments which are essential for achieving positive business results, but until recently did not have equivalents in Russian law. These instruments include, *inter alia*, warranties and representations, indemnities, conditions precedent and covenants. These instruments are necessary to implement the parties' commercial arrangements.

In the last decade, the situation has changed dramatically. First of all, several fundamental changes were introduced into the Russian Civil Code (the RCC) in 2015. These changes implemented in Russian law some legal instruments which have their origin in English law. Secondly, after the beginning of the SMO in February 2022, many international companies left the Russian market and terminated their contractual and partnership relations with their Russian counterparts. Subsequently, many transactions and commercial arrangements are now subject to the law of friendly jurisdictions, but not to English law, which is currently regarded by some lawyers as "toxic" law. In addition, the SMO shifted the focus of foreign investors away from the Russian corporate and financial market. Furthermore, Russian regulators introduced many restrictions on the transactions with residents from unfriendly jurisdictions. As a consequence, the number of contracts subjected to English law has decreased significantly. Finally, the de-offshorisation policy, which was announced before the SMO and has continued since then, resulted in a decrease in the use of offshore holdings and sub-holdings structures by Russian businesses. These relations used to be regulated by English law. This is not the case now.

In this paper, we are going to address these and other related issues.

## **II. Russian Practice of Application of English Contract Law**

### **II.1. Instruments of English Contract Law**

Because of its flexibility and the presence of unique instruments, English law has been widely used by Russian business in order to regulate different types of commercial and corporate relations, specifically financial arrangements, corporate issues, trust and trust-like matters.

Historically, English law played a leading role in the regulation of credit agreements and other financial arrangements. As Russian practice proves, credit and credit facility agreements concluded by Russian banks with foreign banks were traditionally subject to English law. Most, if not all, of these agreements stipulate jurisdiction of foreign arbitration institutions or English courts to consider disputes arising out of such agreements. Before the SMO, Russian courts rarely dealt with these agreements, usually only when such disputes fell under the jurisdiction of Russian courts by default, e.g., when the parties did not stipulate a dispute resolution clause in their agreement or when they decided that it would be easier to claim repayment of the debt from a Russian debtor through a Russian court.

Due to its flexibility, English law allows the parties in financial deals to take into account the particularities of a specific deal and stipulate the requirements necessary to secure repayment of the loan. In particular, the facts which were recognized as established by the contract shall not be proved. This principle is known as “contractual estoppel” and was established in the decision of the England and Wales Court of Appeal in *Springwell Navigation Corporation v. JP Morgan Chase Bank and Others* [2010].<sup>1</sup> In Para. 143 of the decision the court concluded:

“If A and B enter into a contract then, unless there is some principle of law or statute to the contrary, they are entitled to agree what they like. [...] there is no legal principle that states that parties cannot agree to assume that a certain state of affairs is the case at the time the contract is concluded or has been so in the past, even if that is not the case, so that the contract is made upon the basis that the present or past facts are as stated and agreed by the parties.”

The requirements for a loan can be realized by using the concept of conditions precedent, i.e., specific provisions which should be in place in order for a loan to be provided. “Conditions precedent are clauses which provide that certain parts of the contract will only come into force if and when agreed conditions are met. [...] These conditions do not need to be within the control of the parties and do not even need to be

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<sup>1</sup> [2010] EWCA Civ. 1221. Available at: <https://www.bailii.org/cgi-bin/markup.cgi?doc=/ew/cases/EWCA/Civ/2010/1221.html&query=springwell&method=boolean> [Accessed 02.01.2025].

realistic, provided that they are clear and can be objectively assessed” (Ivory and Rogoza, 2012, pp. 18, 19). Such conditions may require the borrower to obtain approval for the transaction from its investment committee and/or major shareholders, or to provide collateral, surety, or any other form of security for the repayment of the loan amount.

The most valuable instruments that have always been in high demand from parties to credit transactions, are warranties & representations, which a borrower should give to a lender. A warranty is a promise that a particular statement made is true at the date of the contract. Warranties are often included in loan and credit agreements, where the borrower assures the lender that the borrowers’ accounts give a true and fair view of the assets and liabilities of the borrowers’ company at a specific date and that the borrower has no outstanding payments and liabilities before any banks, lenders, tax authorities and other creditors (Ivory and Rogoza, 2012, pp. 11, 12). Breach of warranty gives the aggrieved party the right to claim damages but not rescind the contract (Treitel, 2015, Para. 18-042).

Representations are statements made by one party which induce the other party to enter into the contract. In the case of misrepresentation, the aggrieved party may claim rescission of the contract and compensation of damages. The aim of damages is to put the innocent party in the same financial position they would have been in if they had not entered into the contract (Treitel, 2015, Para. 4-005, 20-021). The purpose of warranties and representations is to maintain the status quo in the borrower’s position from the moment of the conclusion of the loan agreement until the moment the parties fulfil their contractual undertakings (Vishnevskij, 2018, p. 111).

Another English law instrument that is common for loan and credit agreements is covenants. A covenant is an agreement or promise from the covenantor to do or refrain from doing something, binding on the person who makes the covenant. They can be positive (e.g., “to provide key financial information to the bank on request”), or negative (e.g., “not to grant new security without the prior consent of the bank”) (Ivory and Rogoza, 2012, p. 20). Covenants are often used in international contracts, but they are only effective if they comply with applicable national law.

## II.2. Remedies for Breach of Contract under English Law

The main remedy available at Common law is damages. The definition of damages is derived from the leading precedent *Robinson v. Harman* [1848], according to which:

“The rule of the common law is that where a party sustains a loss by reason of a breach of contract, he is, so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed.”

This rule allows the aggrieved parties to restore their position and gain compensation for their losses.

Damages in English law are compensatory by their legal nature, because their aim is to restore the situation in which the suffering party would have been in if the breach had not happened. Therefore, the remedies for breach of undertakings under the contract should also be compensatory. This rule was formulated by the Supreme Court of the United Kingdom (the UK) in 2015 in *Bunge SA v. Nidera BV*:

“The fundamental principle of the common law of damages is the compensatory principle, which requires that the injured party is ‘so far as money can do it to be placed in the same situation with respect to damages as if the contract had been performed’: *Robinson v. Harman* [1848] [...]. In a contract of sale where there is an available market, this is ordinarily achieved by comparing the contract price with the price that would have been agreed under a notional substitute contract assumed to have been entered into in its place at the market rate but otherwise on the same terms.”<sup>2</sup>

Hence, the right to claim damages and their amount is predetermined by a comparison between the actual position of the plaintiff after the breach and the position which he had been in before the breach. At the same time, damages are based on the loss of the aggrieved party but not on the gain received by the party in breach<sup>3</sup> (Treitel, 2015, Para. 20-004). According to another principle of recovery of damages, the plaintiff shall not be placed in a better position than he would have been in if the contract had never been breached (Treitel, 2015, Para. 20-

<sup>2</sup> *Bunge SA v. Nidera BV* [2015] UKSC 43.

<sup>3</sup> *Tito v. Waddell (No. 2)* [1977] Ch.106 at 332; *The Solholt* [1983] 1 Lloyd’s Rep. 605 at 608.

007). In *Ruxley Electronics and Construction Co Ltd v. Forsyth* [1996], it was established that “damages are designed to compensate for an established loss and not to provide a gratuitous benefit to the aggrieved party” (Treitel, 2015, Para. 20-007).

According to English law, damages can be in the form of direct loss and loss of profit. Direct loss means non-receipt of the performance under the contract, whereas loss of profit (also known as consequential loss) is the subsequent adverse consequences of such non-receipt (Treitel, 2015, Para. 20-005, 20-025). Direct loss should be awarded either as a “substitute” for the right infringed, or as the cost of performance (Treitel, 2015, Para. 20-005). Thus, loss of profit could be in the form of the interest which a bank or any other creditor would have received if it had placed the funds (which the debtor should have repaid to him) on the financial market. It should be noted that English law allows consequential losses (loss of profits) to be recovered provided that the link between the loss and the breach is not too remote (Treitel, 2015, Para. 20-025). A detailed description of this approach can be found in specialized literature: “In some cases, the claimant reasonably did not borrow replacement money and is entitled, subject to remoteness, to claim the lost profits that would have been made from investing the money that the defendant should have paid the claimant, even if that investment would only have been on deposit in a bank” (Kramer, 2014, Section 7.2).

Russian case law proves that the provisions of English law on damages are applied by Russian state courts to credit and credit facilities agreements. In some instances, English law rules allowed Russian parties to protect their interests against their foreign counterparties.

In the case of *TransKapitalBank JSC (Russia) vs Credit Suisse AG (Switzerland)*,<sup>4</sup> TransKapitalBank joined the credit facility agreement concluded between Credit Suisse and an Uzbek company (the borrower). In the framework of the agreement, TransKapitalBank provided a loan facility to the borrower to the amount of EUR 10 million. The borrower repaid the loan in due course and transferred the amount due and

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<sup>4</sup> Decision by the Arbitrazh Court of the City of Moscow, case No. A40-129186/2022-52-995 dated 10 February 2023. Available at: <http://www.consultant.ru/>. (In Russ.). [Accessed 05.01.2025].

accrued interest to Credit Suisse. The latter, acting as a credit agent, was supposed to transfer these funds to TransKapitalBank, but refused to do so, because on the date of the repayment due (April 2022), the US authorities placed TransKapitalBank on the Specially Designated Nationals and Blocked Persons List (SDN) List.<sup>5</sup> As a result, after April 2022, Credit Suisse refused to transfer the funds to honour its contractual obligations under the credit facility agreement.

The agreement was subject to English law and stipulated the jurisdiction of the London Court of International Arbitration (the LCIA). However, *TransKapitalBank* filed a claim against Credit Suisse to the Arbitrazh Court of the City of Moscow in accordance with Art. 248.1 of the Arbitrazh Code of the Russian Federation (the APC), which gives the Russian state arbitrazh courts exclusive jurisdiction over disputes involving companies and individuals against which a foreign state or international institution has imposed sanctions. The Arbitrazh Court of the City of Moscow assumed its jurisdiction and confirmed that the dispute should be resolved on the basis of English law applicable to the agreement. The court concluded that the defendant failed to prove that they had not been able to fulfill their contractual obligations to remit the funds to the plaintiff. As a Swiss legal entity, Credit Suisse was not obligated to abide by the restrictions imposed on these Russian banks by the US authorities. Voluntary compliance with the sanction rules of foreign states does not release the defendant from liability.

The court asserted that compensation of damages is the main remedy for the breach of contract available at English law. The aim of damages is not to punish the party in breach, but to compensate the losses of the aggrieved party. According to the general principle of English law, compensation of damages is aimed to place the plaintiff in the same situation as if the contract had been duly performed.

In a similar case, *Bank Zenit JSC (Russia) vs Credit Suisse AG (Switzerland)*,<sup>6</sup> *Bank Zenit* provided a loan amounting to USD 20 million

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<sup>5</sup> Specially Designated Nationals And Blocked Persons List (SDN). Available at: <https://ofac.treasury.gov/specially-designated-nationals-and-blocked-persons-list-sdn-human-readable-lists> [Accessed 05.01.2025].

<sup>6</sup> Decision by the Arbitrazh Court of the City of Moscow, case No. A40-121033/2023-52-989 dated 12 December 2023. Available at: <http://www.consultant.ru/>. (In Russ.). [Accessed 05.01.2025].

under a credit facility agreement concluded between *Credit Suisse* and *Intergrain S.A.* (the borrower). In February 2023, the UK Office of Financial Sanctions Implementation HM Treasury (the OFSI) placed *Bank Zenit* on the UK sanctions list.<sup>7</sup> After that, Credit Suisse, acting as a credit agent, refused to transfer the funds to Bank Zenit under the credit facility agreement. The agreement was subject to English law and the disputes should have been referred to the LCIA. Despite the arbitration agreement, in accordance with Art. 248.1 of the APC, Bank Zenit brought an action against Credit Suisse in the Arbitrazh Court of the City of Moscow.

The court concluded that the restrictions imposed on *Bank Zenit* by the OFSI are not mandatory for *Credit Suisse*, as it is a Swiss legal entity, not a UK legal entity. In addition, the UK sanctions do not form part of English contract law chosen by the parties as applicable to their contract (*lex contractus*). Sanction restrictions form part of the personal law of UK companies and individuals (*lex personalies*), but not part of *lex contractus*. Furthermore, the sanction restrictions implemented by the OFCI contradict international law and Russian public policy. Because sanctions are public rules, they do not have any extraterritorial effect and cannot be applied outside the territory of the UK. The court awarded the plaintiff damages in the amount of USD 20 million for breach of contract under English law.

Apart from damages and interest, the aggrieved party may claim the payment of a fixed sum for the breach of contract. Traditionally, English law differentiated between penalty clauses, which are invalid, and liquidated damages clauses, which are generally upheld (Treitel, 2015, Para. 20-129).

It was stated in the leading case of *Dunlop vs New Garage Ltd* [1915] that if a sum for breach of contract is of an unconscionable amount, it will be considered penal and unenforceable. The court will strike out the penalty clause entirely and will not adjust it with a lower sum. If the clause is a “genuine” attempt by the parties to estimate in advance the loss which would result from the breach, it is a liquidated damages clause (Treitel, 2015, Para. 20-130, 20-131).

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<sup>7</sup> UK Sanctions List. Last Updated: 28.02.2025. Available at: <https://www.gov.uk/government/publications/the-uk-sanctions-list> [Accessed 06.03.2025].

A valid liquidated damages clause is one where: (a) an agreed sum constitutes a genuine pre-estimate of the loss from breach, (b) there is an intention on the part of the parties to calculate losses in advance, (c) the amount of damages is reasonable.

A typical liquidated damages clause is as follows:

“[...] therefore, the Contractor shall be liable to the Owner for payment of liquidated damages to the amount of \$ 1,000 for each day that substantial completion is delayed beyond the contract time. Such liquidated damages are intended to represent estimated actual damages and are not intended as a penalty [...].”

Furthermore, in two famous cases *Cavendish Square Holding BV v. Talal El Makdessi* [2015] and *ParkingEye Ltd v. Beavis* [2015] (Treitel, 2015, Para. 20-138), it was established that remedies are not penalties if they are (i) not “out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation”; (ii) not extravagant; and (iii) not intended to punish the party.

### III. Failure to Fulfil Contractual Obligations and Sanctions

#### III.1. Principle of Strict Liability

A breach of contract is committed when a party, without lawful excuse, fails or refuses to perform what is due from him under the contract or improperly performs his obligations. Suggested: In the event of a breach, the aggrieved party may pursue one of several remedies, including claiming damages, seeking payment of an agreed sum, requesting specific performance of the contract, or obtaining an injunction (Treitel, 2015, Para. 17-049).

English law supports the principle of “strict liability.” “The most obvious illustration of this principle is provided by the case of a buyer who cannot pay the price because his bank has failed or because his expectation of raising a loan has not been fulfilled, or because he is prevented by exchange control regulations from remitting money to the place where he has agreed to pay, or because his supply of the currency in which he has agreed to pay has become exhausted and cannot be replenished. In such cases, there is no doubt that he is liable: inability

to pay money, even if it occurs entirely without the fault of the party who was to make the payment, is not an excuse for failing to make the payment” (Treitel, 2015, Para. 17-065). These rules were established in *Universal Corp v. Five Ways Properties Ltd* [1979] and *Congimex SARL (Lisbon) v. Continental Grain Export Corp (New York)* [1979]. “The principle of strict liability may be modified by the terms of the contract (e.g., by a “force majeure” clause), but unless this is done, liability is quite independent of fault” (Treitel, 2015, Para. 17-065).

It should be noted that the principle of strict liability was applied by the Russian courts in the aforementioned cases (*TransKapitalBank* and *Bank Zenit*). Specifically, the refusal of Credit Suisse, who was acting as a credit agent, to honor their payment obligations to the Russian banks constituted a breach of the principle of strict liability established by English law.

According to the judgement in *Bank Zenit JSC vs Credit Suisse AG*, the reference of the defendant (*Credit Suisse*) to the fact that they could not fulfill their obligations because of Bank Zenit was included on the OFCI sanction list was not valid, since Credit Suisse is a Swiss legal entity. The inclusion of the bank on this list did not constitute a force majeure event either. The court cited McKendrick, saying that in accordance with current doctrine the concept of force majeure is alien for English law (McKendrick, 2013, p. 5).

### **III.2. Doctrine of Frustration and Sanctions**

According to common law of contract, liability for non-performance of the contractual obligations is strict. Except in certain cases, non-performance of contractual obligations constitutes a breach of contract, granting the aggrieved party the right to claim damages (McKendrick, 2013, p. 3). The substantiation of this rule was given by the Court of King’s Bench in 1647 in *Paradine v. Jane*:

“When the party by his own contract creates a duty or charge upon himself, he is bound to made it good, if he may, notwithstanding any accident by inevitable necessity, because he might have provided against it by his contract” (McKendrick, 2013, p. 3).

Currently, common law allows obligors to be released from liability for failure to perform their contractual duties in certain cases. Specifically, such an excuse is possible under the doctrine of frustration. The leading precedent in this field is *Davis Contractors Ltd. v. Fareham U.D.C.* [1956], according to which the doctrine of frustration excuses non-performance where “a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract” (McKendrick, 2013, p. 5). However, the terms of the contract are *prima facie*<sup>8</sup> absolute. “It is not surprising that judges are nowadays generally reluctant to find that a particular contract has been frustrated” (McKendrick, 2013, p. 5).

Some foreign creditors have tried to invoke the doctrine of frustration to justify their refusal to fulfill their contractual obligations before Russian banks which are included on sanction lists. Some lawyers try to justify non-performance by reference to the arguments in *Ralli Bros v. Compania Naviera Sota y Aznar* [1920] where the English court established a common law rule that “where an act required by a contract to be performed in a foreign country becomes illegal under that country’s law, the contractual obligation to perform that act is discharged” (Chitty, 2018, Para. 30-360). However, the factual matters in this case are fundamentally different from the cases reviewed by Russian courts. Specifically, the payments which had to be made by the credit agent (Credit Suisse) to the Russian banks were not illegal under either Russian or Swiss law.

The doctrine of frustration of the contract was consolidated by Lord Radcliffe in *Davis Contractors Ltd v. Fareham UDC* [1956]: “Frustration occurs whenever the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. *Non haec in foedera veni*. It was not this that I promised to do” (McKendrick, 2013, pp. 38–39; Symons and Dalby, 2022, p. 176).

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<sup>8</sup> Lat. — based on the first impression; accepted as correct until proved otherwise.

Further, in *Tsakiroglou & Co. Ltd. v. Noblee & Thorl, G.m.b.H.*<sup>9</sup> and *Ocean Tramp Tankers Corporation v. V/O Sovfracht (The Evgenia)*<sup>10</sup> the courts came to the conclusion that hardship in performance of a contract does not make the contract frustrated. In the case of *Tsakiroglou*, a contract was made for the sale of groundnuts to be delivered from Sudan to Hamburg. When the contract was made both parties expected that shipment would be via Suez, but this was not stated in the contract. The court held that the contract was not frustrated by the closure of the Suez Canal, and that the seller ought to have shipped the goods via the Cape of Good Hope. Although this would have taken two and a half times as long as shipment via Suez and would have doubled the cost of carriage, the difference between the two methods of performance was not sufficiently fundamental to frustrate the contract. In other cases related to Suez,<sup>11</sup> the courts also arrived at the conclusion that the difference between the two methods of delivery (i.e., via the Suez Canal or via the Cape of Good Hope) was not fundamental enough to claim frustration of contracts (Treitel, 2015, Para. 19-031).

In *British Movietonews Ltd v. London and District Cinemas*,<sup>12</sup> considered by the House of Lords, Lord Simon said:

“The parties to an executory contract are often faced, in the course of carrying it out, with a turn of events which they did not at all anticipate — a wholly abnormal rise or fall in prices, a sudden depreciation of currency, an unexpected obstacle to the execution, or the like. Yet this does not in itself affect the bargain which they have made” (Treitel, 2015, Para. 19-005).

As it follows from the aforementioned cases, English law is based on the assumption that termination of a contract due to impossibility of performance (frustration) is available only if the change of circumstances became so significant that it made the performance of the contract impossible or illegal for the party. The parties are expected to foresee the occurrence of certain negative scenarios, such as strikes, wars or price

<sup>9</sup> [1962] A.C. 93.

<sup>10</sup> [1964] 2 Q.B. 226.

<sup>11</sup> *Glidden v. Hellenic Lines Ltd* 275 F. 2d. 253 (1960); *Transatlantic Finance Corp v. USA* 363 F.2d 312 (1966); *The Captain George K* [1970] 2 Lloyd's Rep. 21.

<sup>12</sup> [1952] A.C. 166 at 185.

fluctuations, and they should not refer to the doctrine of frustration just because the performance has become more burdensome than was anticipated at the time of the conclusion of the contract (McKendrick, 2013, p. 43).

The Arbitrazh Court of the City of Moscow applied this rationale in the cases of *TransKapitalBank* and *Bank Zenit vs Credit Suisse*. In both cases, the place of performance of payment was located in Switzerland (the place from which the payment should have been made by the credit agent (Credit Suisse)), and in Russia (the place where the relevant Russian bank (a creditor) should have received the money). According to the agreements, the payments should have been made in USD, and such payments should have been cleared through the Bank of New York Mellon. These payments, if they had been made, could have potentially been blocked. However, according to the credit facility agreements, the places for performance of the contractual undertakings were outside the US. Therefore, the credit agent could not refer to impossibility or illegality of performance in the place where these obligations should be performed, i.e., in Russia and Switzerland. As a result, rescission of the agreements due to impossibility of performance (frustration) was not an available remedy in these cases.

It should be noted that the illegality of performance due to sanctions imposed on the bank was discussed in a leading case in this area — *Libyan Arab Foreign Bank v. Bankers Trust Co* [1989].<sup>13</sup> However, this issue deserves separate consideration and we will not discuss it here.

From the perspectives of English law, the refusal of the credit agent (Credit Suisse) to transfer the funds received from the borrower to the creditor (*TransKapitalBank* and *Bank Zenit*) due to decision of the credit agent to voluntarily follow the OFAC and OFSI sanction rules does not release the credit agent from liability for failure to perform the credit facility agreements. Other sanction risks, specifically the risks of secondary sanctions being imposed by the US authorities, may release a party from performance of the contract only if it is specifically stated in the contract itself. Such a rule of English law was established in *Lamesa Investments Limited v. Cynergy Bank Ltd* [2020]<sup>14</sup> (Treitel, 2015,

<sup>13</sup> Q.B. 728.

<sup>14</sup> EWCA Civ 821.

Para. 19-036). Normally, credit facility agreements are only concerned with the obligations of the creditor, borrower and other obligors. They do not usually grants the credit agent the right to refuse payment to a creditor due to the fact that the latter has been included on sanction lists.

In English law, “a contract may be discharged if it provides for a method of performance which becomes impossible” (Treitel, 2015, Para. 19-030). Thus, in *Nickoll & Knight v. Ashton Edridge & Co* [1901] a contract stipulated that goods should be “shipped per steamship Orlando from Alexandria during [...] January.” The Orlando later ran aground in the Baltic, so she could not get to Alexandria in January. It was held that the contract was frustrated since it was to be construed as providing for performance only in the stipulated manner (Treitel, 2015, Para. 19-030).

However, there is another general rule in English contract law which states that if a supervening event makes one of alternative performances, provided by the contract, impossible or illegal, the contract is not discharged so long as another alternative remains possible and lawful.<sup>15</sup> English law does not allow the court to amend or put an end to the contract simply because the contract has become more onerous as a result of supervening events. As was seen above in the *case of the Tsakiroglou*, English courts are very hesitant to invoke the doctrine of frustration in cases other than of impossibility (Smits, 2021, p. 202).

Therefore, the risk of secondary sanctions being imposed on the credit agent by the US authorities could be mitigated or overcome by changing payment from USD to another currency upon the parties’ agreement if they are willing to do so. Nevertheless, even if we apply the rule that the contract should be performed exactly in the way the parties agreed to (*Nickoll v. Ashton*), a fear of secondary sanctions does not constitute a reasonable ground for non-performance.

In the above-mentioned cases, which were under the consideration of Russian courts, the credit agent was not bound by any specific method of performance of the contract in accordance with the relevant

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<sup>15</sup> *Barkworth v. Young* (1856) 1 Drew. 1 at 25; *Reardon Smith Line Ltd v. Ministry of Agriculture; Fisheries and Food* [1963] A.C. 691 at 730; Treitel, Para. 19-053.

credit facility agreement. A substituted or alternative method, such as payment in euros or pounds, could not be radically different from the method stipulated by the credit facility agreement, i.e., payment in USD. Therefore, there was no grounds for application of the doctrine of frustration by the court.

#### **IV. Influence of English Law on Russian Contract Law**

As a result of the high demand for English contract law instruments from Russian parties, it was decided to introduce certain English law instruments into the Russian legal system. The respective amendments were included in the RCC in 2015. They concern conditional contracts, representations (“zavereniya”), waivers, indemnities (compensation of losses), irrevocable power of attorneys and others. We will briefly consider some of these recent developments below.

First of all, some elements of the concept of warranties and representations were promulgated in Art. 431.2 of the RCC. This Article provides that a party is liable for any statement (“zaverenie”) which relates to circumstances relevant to entering into a contract if that representation is untrue. Such representation (“zaverenie”) may relate to the subject matter of the contract, authority to enter into the contract, existence of licenses, a party’s financial status, etc. For the breach of such a statement (“zaverenie”), the aggrieved party may claim either (a) damages or (b) a penalty. If the representation was essential but it was not true, the aggrieved party may also claim (c) rescission of the contract.

It should be noted that the concept of “zaverenie” under Russian law combines characteristics of both warranties and representations under English law. Thus, for breach of “zaverenie,” the aggrieved party may claim both damages and rescission of the contract, which is common remedy for the breach of representations but not warranties under English law. In addition, English law does not provide such a remedy as a penalty for the breach of either warranties or representations, whereas “zaverenie” does. Finally, “zaverenie” could be a statement about the facts (which is a characteristic of a warrantee under English law). “Zaverenie” could be also a statement which induces the other party

to enter into agreement (which is a characteristic of a representation under English law). In sum, the Russian concept “zaverenie” does not provide a distinction between warranties and representations as they are understood in English law. In fact, it does not make any difference between warranties and representations and covers both concepts.

Amendments were also introduced in the RCC regarding conditional contracts to make them closer to international practice, specifically to the English concept of conditions precedent. Traditionally, Russian law recognized conditional contracts, but the conditions had to be outside the control of the parties. If the conditions were within the control of the parties, this contract was never made. After the introduction of the respective amendments in 2015, the new approach is that Russian law does recognize conditional contracts, even if the conditions are within the control of the parties. Even in such a case, the contract is considered formed, valid and enforceable. Article 327.1 of the RCC introduces a concept similar to conditions precedent. It provides that the fulfillment of obligations (and the exercise, modification and termination of certain rights under a contractual obligation), may be conditioned by (a) the performance or non-performance of certain actions by one of the parties of the obligation or (b) the occurrence of other circumstances stipulated by the contract, including those fully dependent on the will of one of the parties.

As regards covenants, unlike English law, Russian law is still developing in this area. Positive covenants should be enforceable as they are treated as an obligation by the courts. Negative covenants are not permitted since, according to the general principle, a party cannot waive its right to do something, except for some exclusions (Ivory and Rogoza, 2012, p. 21). This general rule is established by Art. 9 of the RCC which provides that “A waiver of rights does not result in termination of these rights.” The exception from this general rule is provided by Art. 450.1 of the RCC, according to which, “A party to a contract may waive a certain right under the contract.” This rule applies only to individuals and companies involved in entrepreneurial activities. Russian practice proves that liability waivers are permissible provided that they are (a) specific and do not release the party from liability in general, (b) are limited to entrepreneurial activity, and (c) they concern contractual

rights only. Covenants are now used in agreements subjected to Russian law. Provided that certain conditions are met, they are recognized as valid by Russian courts (Ushakov and Haraeva, 2013, p. 161).

One of the most popular instruments in the commercial world is an irrevocable power of attorney, which was introduced in the RCC in 2013 (Art. 188.1 of the RCC). This power of attorney (PoA) secures the fulfilment of specific contractual duties by the parties. It empowers an attorney to act in their own interests, and sometime against the interests of a principal (an issuer of the PoA), who may not revoke the PoA and needs to follow the rules agreed upon by the parties.

This instrument is widely used in English governed contracts, specifically in share purchase agreements (SPA) and credit agreements when a debtor's PoA authorises the creditor to sell the debtor's assets in order to fulfill the debtor's obligations to repay a loan. After 2013, Russian governed contracts often require a party (e.g., a seller in the SPA) to issue an irrevocable PoA. The introduction of these rules on an irrevocable PoA into the Russian legal system was initiated by the Working Group for the Creation of the International Financial Center in Moscow. Initially, this initiative caused certain concerns, but still was implemented (Vitryanskiy, 2018, p. 20).

Another English contract law instrument which plays a significant role in corporate transactions is put and call options. Under English law, "a put option is a right or option conferred on one party to require another to compulsorily purchase an asset (for example, shares) under the terms of a pre-agreed contract," whereas "a call option is the right for one party to require another party to sell its shares for a pre-determined price" (Ivory and Rogoza, 2011).

Until recently, Russian law did not properly address the regulation of such issues and there were reasonable doubts as to whether or not put and call options were enforceable. In 2015, provisions on option agreements were introduced into the RCC. According to Art. 429.2 of the RCC, an option agreement is one which provides an irrevocable offer for the party to conclude one or several agreements on the conditions stipulated by the option agreement. Under Art. 429.3 of the RCC, under an option agreement, one party may require another party to undertake certain actions, such as to make a payment or accept assets, under

conditions provided by the option agreement. Option agreements are widely used in shareholder arrangements, which are now often subject to Russian law.

Apart from the above-mentioned institutions, Russian law also accepted other legal concepts which we will not consider here in detail. Some of these concepts are the product of international and domestic business practice, but most of them have their origin in English contract law.

### **V. The Prospects of Using English Law by Russian Courts**

English contract law has proved its efficiency and relevance in regulating international business transactions with Russian parties. Now, we are going to consider the factors which undermine the prospects of the use of English law in Russia.

The first factor is the Western sanction policy and Russian anti-sanction measures which were launched as a result of the SMO started in February 2022. Today, most Russian businesses prefer not to subject their contracts to English law and the jurisdiction of English courts. The usual explanation for this is that they try to avoid difficulties in hiring English counsel and paying for their services. The companies associated with the Russian state (some of which have been placed on the US, EU and UK sanction lists) are also afraid of unfair treatment in English courts.

The second factor is the de-offshorization policy, which started with the introduction of the rules on controlled foreign companies (CFC rules) in the Russian Tax Code in 2014 (these rules have been in effect since 2015). It is a well-known fact that for many years before the SMO, English law was actively used by Russian businesses and their foreign counterparts to regulate their M&A transactions, shareholder and share purchase agreements. These deals used to be structured through offshore jurisdictions. Russian courts rarely dealt with these corporate law matters and trust arrangements since the respective contracts traditionally referred all disputes to international arbitrations or English courts. The de-offshorization policy, and the countermeasures adopted by the Russian authorities, have limited the practice of using

offshore holding and sub-holding companies by Russian businesses. Such structures are still used but not on such a scale as before February 2022.

Finally, several amendments introduced in the RCC have made Russian law more attractive to Russian businesses and reduced their dependence on English law. In other words, as more English law instruments are introduced into the Russian legal system, the more contracts are subject to Russian law by the respective parties.

Unfortunately, current Russian court practice also has examples of negative treatment of English contract law. In a number of cases, Russian courts refused to apply English law that should have been applicable by virtue of the contractual choice of law clause. In the case of *Sovcombank (Russia) vs Citybank N.A. (USA) & Citybank JSC (Russia)*,<sup>16</sup> a swap contract was subject to English law. However, the court refused to apply this foreign law because it allegedly contradicted Russian public policy (Art. 1993 of the RCC). According to the judgement, Western economic sanctions cannot justify the violation of the rights of a Russian legal entity, including any violation which was committed by way of unilateral rescission of a contract.

In the case of *Gasenergobank JSC (Russia) vs UBS (Switzerland)*,<sup>17</sup> a plaintiff joined a credit facility agreement concluded between a defendant and a third entity (a borrower). The defendant, acting as a credit agent, was supposed to transfer the funds he received from the borrower to the plaintiff, but refused to do so, because the plaintiff was placed on the SDN List. It is worth noting that the facts of this case were similar to those in the cases of *TransKapitalBank* and *Bank Zenit vs Credit Suisse* that we have already analysed in this paper. In all these cases, the credit facility agreements were subject to English law. However, in the case of *Gasenergobank*, the court did not apply English law and did not provide any reasons for this. Instead, the court applied

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<sup>16</sup> Decision by the Arbitrazh Court of the City of Moscow, case No. A40-167352/23-3-1320 dated 17 October 2023. Available at: <http://www.consultant.ru/>. (In Russ.). [Accessed 31.03.2025].

<sup>17</sup> Decision by the Arbitrazh Court of the City of Moscow, case No. A40-155943/23-3-1228 dated 23 October 2023. Available at: <http://www.consultant.ru/>. (In Russ.). [Accessed 31.03.2025].



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