FEDERAL ARBITRAZH COURT FOR THE NORTH-WESTERN DISTRICT

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RESOLUTION

10 May 2011

Case No. A56-68936/2010

The Federal Arbitrazh Court for the North-Western District composed of the presiding judge S.V. Afanasyev, judges K.Yu Korobov and O.Yu Nyefyedova.

Present on behalf of the company Borregaard Indastries Ltd, F.G. Belykh (under power of attorney of 28 April 2011) and I.E. Kokin (under power of attorney of 20 January 2011), on behalf of the open joint stock company "Vyborg Cellulose", P.S. Voyushin (under power of attorney of 26 July 2010).

Having examined at the open hearing of 5 May 2011 the cassation complaint of the open joint stock company Vyborg Cellulose against the ruling of the Arbitrazh Court of Saint-Petersburg and the Leningrad Region of 3 March 2011 in Case No. A56-68936/2010 (judge E.V. Savina),

established:

Company Borregaard Indastries Ltd created under the laws of England and Wales and doing business in Norway (hereinafter – "the Company") filed with the Arbitrazh Court of Saint Petersburg and the Leningrad Region an application for recognition and enforcement of the award of 30 September 2010 rendered by the Arbitration and Dispute Resolution Institute of the Oslo Chamber of Commerce (hereinafter – "the Arbitration Tribunal") ordering the open joint stock company "Vyborg Cellulose" of the Russian Federation (hereinafter – "the Firm") to pay to the applicant USD 4 788 000 with interest on this amount, according to Article 2 of the Norwegian Law on Charging Interest, starting from 31 May 2010 until the date of full payment, as well as NOK 1 200 000 in compensation for the applicant's expenses related to the arbitration proceedings and EUR 100 000 in compensation for the debtor's share of arbitrators' costs and expenses.

The Firm was joined to the proceedings as an interested party.

By a ruling of 3 March 2011 the application of the Company was granted.

In the cassation complaint the Firm requests to cancel the ruling of 3 March 2011 and to reject the Company's application.

In support of the cassation complaint the applicant argued the following:

- the Arbitral Tribunal in awarding interest applied Norwegian substantive law in violation of terms of the arbitration agreement;
- the court of first instance disregarded established judicial and arbitral practice of proportionality between liability and infringement, it did not take into account that the penalty awarded by the Arbitral Tribunal was of punitive and not of compensatory character;
- the court of first instance in the challenged ruling violated Articles 15 and 170 of the Arbitrazh Procedure Code of the Russian Federation (hereinafter – "RF APC") failed to state reasons for which it rejected the arguments of the Firm provided in written submissions.

In response to the cassation complaint, the Company alleged that these arguments were groundless and requested to uphold the ruling of 3 March 2011.

At the court hearing, the representative of the Firm sustained the cassation complaint and the representatives of the Company objected to it.

The legality of the challenged ruling is examined in the cassation review.

Pursuant to paragraphs 2.1-3.1.1. of the supply contract dated 19 April 2006 No. 539/06 (hereinafter – "the Contract"), the Firm (supplier) undertook to supply for a period of 10 years, 35 000 tons of lignin yearly, and the Company (buyer) to accept and pay for it a price of USD 152 per ton agreed for 2006 and 2007.

According to paragraph 10.3 of the Contract, to allow for unilateral termination, the party breaching the terms of Contract should be notified in writing. If non-performing party fails to remedy the breach within 30 days from the date of the written notification, the other party is entitled to terminate the Contract.

According to paragraph 10.4 of the Contract, each party is entitled to unilaterally refuse to perform the terms of contract without giving reasons by sending a written notice to the other party no less than by 30 calendar days in advance. In such cases that the party requesting the termination of the Contract is bound to make an advance payment in the amount of USD 5 320 000. If the Contract is terminated during the following years, the above amount of compensation shall be diminished yearly by 10% (USD 532 000) starting from the first year of contract.

Paragraph 14.2.3 of the Contract provides that if a dispute could not be settled through mediation within 60 days from the receipt of request from a party and the parties do not agree to extend this period, the dispute shall be settled by the Arbitral Tribunal according to its rules. The number of arbitrators shall be three.

As it appears from the case materials, the parties to the Contract increased the price of supplied goods to USD 162 from 1 January 2007 and to USD 177 from 1 March 2007.

As a result of the Company's rejection of the Firm's offer to again increase the price of the supplied lignin to USD 294, the latter ceased to perform its obligation to deliver goods.

By letter of 7 May 2007, the Company notified the Firm of the violation of terms of lignin supply Contract.

As lignin supply did not resume, on the 27 June 2007 the Company notified the Firm in writing of the termination of the Contract; on 5 March 2008 it requested the Oslo Chamber of Commerce to settle the dispute through mediation and on 27 October 2008 it filed a lawsuit against the Firm to recover USD 4 788 000 provided for by paragraph 10.4 of the Contract.

The Arbitral Tribunal, composed of Robert Mattson, Viggo Hagstrøm and V.A. Musin, by an award of 30 September 2010 ordered the Firm to pay the Company USD 4 788 000 with interest on this amount according to Article 2 of the Norwegian Law on Charging Interest, starting from 31 May 2010 until the date of making of a full payment, and NOK 1 200 000 to compensate the applicant's expenses related to the arbitration proceedings, EUR 100 000 to compensate for the debtor's share of arbitrators' costs and expenses.

As the Firm did not voluntarily comply with the award of the Arbitral Tribunal which entered into force, the Company filed this application with an arbitrazh court.

According to Article 6(3) of the Federal Constitutional Law of 31 December 1996 No 1-FKZ "On Judicial System of the Russian Federation", the compulsory nature of resolutions of foreign courts, international courts and arbitral tribunals shall be determined by the international treaties of the Russian Federation.

Pursuant to Article 241(1) RF APC, awards of courts of arbitration and international commercial arbitral tribunals, rendered in the territories of foreign States in disputes and other matters arising from the conduct of an entrepreneurial or other economic activity (foreign arbitral awards), shall be recognized and enforced in the Russian Federation by the arbitrazh courts if the recognition and enforcement is envisaged by an international treaty of the Russian Federation and federal legislation.

The procedure for recognition and enforcement of foreign arbitral awards is provided by the New York Convention of the United Nations "On the Recognition and Enforcement of Foreign Arbitral Awards" of 10 June 1958 (hereinafter – "the Convention") to which the Russian Federation and Norway are parties.

Pursuant to Article III of the Convention, the Russian Federation recognizes arbitral awards as binding and enforces them in accordance with the domestic rules of procedure, under the conditions laid down in the Convention.

In accordance with Article V of the Convention, the recognition and enforcement of the award may be refused in cases where a party against which the award is rendered furnishes, to the competent court where the recognition and enforcement is sought, proof that:

(a) the parties to the agreement 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

(b) the party against whom the award is rendered was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

(c) the award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, or

(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; or

(e) the award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made (paragraph 1).

In addition, the competent court has the authority to refuse the recognition and enforcement of the arbitral award in cases where (a) the subject matter of the difference is not capable of settlement by arbitration under the law of that country; or (b) the recognition or enforcement of the award would be contrary to the public policy of that country (paragraph 2).

Analogous principles were enshrined in Article 36(1) of the Law of the Russian Federation of 7 July 1993 No 5338-1 "On International Commercial Arbitration" (hereinafter – "Law No 5338-1").

Article 244(2) RF APC specifies that an arbitrazh court shall refuse, entirely or in part, recognition and enforcement of a foreign arbitral award on grounds provided for in paragraph 7 of Article 244(1) and Article 239(4) RF APC for refusing the issuance of an enforcement writ for coercive enforcement of an award of an international commercial arbitral tribunal, unless otherwise provided by an international treaty of the Russian Federation.

By virtue of Article 243(4) RF APC the arbitrazh court is not allowed to review a foreign award on the merits.

As it is apparent from the case materials, the Firm has not presented the court with evidence that the grounds provided in Article V(a)-(e) of Convention for refusing the recognition and enforcement of this arbitral award on the territory of the Russian Federation existed.

Objecting to the recognition and enforcement of the award rendered by the arbitral tribunal and in reply to the Company's application and the cassation complaint, the Firm asserts that the award violated fundamental principles of Russian law. It argued that, on the one hand, it did not contain references to rules of Russian substantive law governing the recovery by the Company of USD 4 788 000, and on the other hand in computing interest, the reference was made to the Norwegian Law on Charging Interest, which was contrary to paragraph 14.1 of the Contract. In addition, according to the Firm, the compensation awarded was disproportionate to the obligation breached.

These arguments presented by the Firm are groundless in light of the following:

Article 1186(1) of the Civil Code of the Russian Federation (hereinafter – "RF CC") provides that the law applicable to civil relations that involves foreign citizens or foreign legal entities or civil relations encumbered by another foreign factor, including cases when the object of civil rights is located abroad, shall be determined on the basis of international treaties of the Russian Federation, the Civil Code of the Russian Federation, other laws (Article 3(2) RF CC) and the usages recognised in the Russian Federation. Moreover, peculiarities of determining the law applied to international commercial arbitration shall be established by the law on international commercial arbitration.

Article 28 of the Law No. 5338-1 provides that the arbitral tribunal shall decide the dispute in accordance with the substantive laws chosen by parties (paragraph 1). In addition, in all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the trade usages applicable to the transaction (paragraph 3).

The parties to the Contract agreed that its interpretation, validity and performance shall be governed by the laws of the Russian Federation (paragraph 14.1).

As is apparent from the award, the Arbitral Tribunal decided the dispute between the Company and the Firm on the basis of Russian federal laws of 26 December 1995 "On Joint Stock Companies" (No 208-FZ), 26 July 2006 "On Protection of Competition" (No 135-FZ) and the Civil Code of the Russian Federation.

In particular, in awarding compensation to the Company, the Arbitral Tribunal relied on paragraph 10.4 of the Contract as well as the provisions of the Civil Code of the Russian Federation,

agreeing with the opinion of Professor A.P. Syergyeyev acting in the capacity of an expert on Russian law, who noted that disputed legal relations were governed by Articles 309, 310, 393, 396 and 401 of the RF CC (paragraphs 8.1.1, 8.2.6 of the arbitral award, paragraphs 8.1-8.13 of the expert opinion on issues related to the application of the Russian legislation).

The application by the Arbitral Tribunal of the referred provisions of the Russian substantive law as well as the terms of the Contract cannot be considered as violating the public policy of the Russian Federation.

The Firm's argument that the awarded compensation was disproportionate to the obligation breached should be rejected by the court of cassation instance on the following grounds:

According to Article 330(1) RF CC, the penalty or fine shall be defined as the sum of money, determined by law or by agreement, which the debtor is obliged to pay to the creditor in case of non-performance, or an improper performance, of the obligation, in particular, in case of delay of performance. When seeking the payment of penalty from a party, the creditor is not obliged to provide evidence of loss suffered by it.

Pursuant to Article 394(1) RF CC, if a penalty is imposed for non-performance, or an improper performance of an obligation, the losses shall be compensated in the part not covered by the penalty.

Pursuant to Article 1(1) RF CC, one of the basic principles of the civil law is to recognize the equality of parties in their legal relations and provide remedies to restore their breached rights.

On the basis of the legal position formulated in paragraph 29 of the Information Letter of the Presidium of the Highest Arbitrazh Court of the Russian Federation No. 96 of 22 December 2005 entitled "Review of Practice of the Arbitrazh Courts' Decisions in Cases for Recognition and Enforcement of Foreign Courts' Decisions, Challenges to Arbitral Awards and Issuance of Enforcement Writs for the Coercive Enforcement of Arbitral Awards", public policy is based on principles of equality of parties in civil law relations, adequacy between the civil liability and consequences of infringement, taking the fault into account.

Therefore, the civil legislation of the Russian Federation is premised on the principle of equality of rights and obligations of the Russian and foreign legal entities and natural persons, and envisages charging the penalties as a potential liability measure for non-performance or inappropriate performance of obligations under a contract. Consequently, the penalty is part of the legal system of the Russian Federation and its recovery cannot be in breach of the public policy of the Russian Federation.

The Firm did not prove this and it does not result from the case that the measures of civil liability applied by the arbitral tribunal were disproportionate to the consequences of the breach of the Contract.

In such circumstances, the Arbitral Tribunal ordering the Firm to pay the Company the penalty provided for by the Contract does not violate public policy of the Russian Federation.

Concerning the application by the Arbitral Tribunal of the Norwegian Law on Charging Interest on accrual of interest on the amount of compensation awarded to the Company due to the termination of the Contract, the court of cassation instance notes the following.

From the award it is clear that the Company as well as the Firm insisted on the application of the Norwegian Law on Charging Interest to accrual of interest on the amounts claimed.

The interest has been computed by the Arbitral Tribunal on the basis of the above law, not in order to impose an additional liability on the firm for nonperformance of a monetary obligation but for indexation of the awarded amounts.

The provision of the Norwegian Law on Charging Interest providing for indexation of the awarded amounts by charging interest is analogous to Article 183 RF APC and is a procedural not a substantive law rule.

As the parties to the Contract only agreed on the applicable substantive law, the Arbitral Tribunal relying on Article 6 of its rules was entitled to base its decision on the Norwegian Law on Charging Interest.

Taking the foregoing into account, the court of first instance rightly granted the application.

The fact that the court of first instance considered the objections of the Firm to the Company's application untenable without giving reasons thereto cannot serve as a basis for reversal of a correct judicial act.

In these circumstances there is no ground for granting the cassation complaint.

Because the cassation complaint was rejected, the stay of enforcement of the ruling of 3 March 2011 granted by the ruling of the Federal Arbitrazh Court for the North-Western District of 1 April 2011 shall be lifted.

Based on Articles 286, 287, 289, 290 of the Arbitrazh Procedure Code of the Russian Federation, the Federal Arbitrazh Court for the North-Western District

RESOLVED:

The ruling of the Arbitrazh Court of Saint Petersburg and the Leningrad Region in the case No. A56-68936/2010 of 3 March 2011 shall be upheld and the cassation complaint of the open joint stock company Vyborg Cellulose be dismissed.

The stay of enforcement of the ruling of Arbitrazh Court of Saint Petersburg and the Leningrad Region of 3 March 2011 in the case No. A56-68936/2010 granted by the Federal Arbitrazh Court for the North-Western District of 1 April 2011, shall be lifted.

Presiding judge: S.V. Afanasyev

Judges K.Yu Korobov

O.Yu Nyefyedova