

Client Update

Russian Supreme Court Rules Lessor Could Not Withdraw Consent to Property Sublease

The Chamber for Commercial Disputes of the Supreme Court of the Russian Federation (the “Russian Supreme Court”) recently ruled that a lessor could not unilaterally withdraw its consent to the sublease of property by the lessee, which is a significant disputed issue for the commercial real estate lease market.¹ Consideration of this case has revealed inconsistencies between different court instances in their approach. The Russian Supreme Court’s decision is expected to influence how the terms, form and procedure for granting of the lessor’s consent to the sublease of property will be reflected in lease agreements.

FACTS OF THE CASE

In accordance with the terms of the lease agreement, the lessee was granted the right to assign the lease agreement to another party, sublease the leased premises, pledge the lease rights and contribute the lease rights to the authorized capital of legal entities. After the execution of the lease agreement the lessee subleased the premises to third parties.

The lessor gave the lessee notice with reference to Article 157.1 of the Civil Code of the Russian Federation (the “Russian Civil Code”) withdrawing its consent to the sublease of the leased premises. Because the lessee continued to sublease the premises after the lessor had withdrawn its consent to such sublease, the lessor proposed to terminate the lease agreement.

The lessee did not agree with such rationale for termination of the agreement, and the lessor filed a lawsuit to terminate the agreement with reference to material breach of the agreement by the lessee (para. 2, Article 450 of the Russian Civil Code).

¹ Ruling of the Supreme Court of the Russian Federation dated January 22, 2018 in Case No. 303-ЭС17-13540.

FINDINGS OF THE COURT OF THE FIRST INSTANCE, THE COURT OF APPEAL AND THE COURT OF CASSATION

The court of the first instance (the Arbitrazh Court of the Khabarovsk Region)² and the court of appeal (the Sixth Arbitrazh Court of Appeal)³ refused to terminate the lease agreement due to the following circumstances:

- The lessor's notice of withdrawal of its consent to the sublease of property is a statement of material amendment of the lease agreement, as a result of which the lessee loses what it expected to receive upon execution of the agreement. However, material amendment of the agreement is possible either upon agreement of the parties or by court judgment (para. 1, Article 450 of the Russian Civil Code).
- The lessor's unilateral statement on withdrawal of its consent to the sublease of property according to Article 157.1 of the Russian Civil Code is an abuse of the right.

When considering the case in cassation, the *Arbitrazh* Court of the Far Eastern District delivered a completely opposite ruling, overturning the judgments of the court of the first instance and the court of appeal, thereby satisfying the claim on termination of the lease agreement.⁴ The court of cassation relied on the following arguments:

- Provisions of para. 2, Article 615 of the Russian Civil Code are mandatory and do not allow conditions to be placed on the requirement that the lessee obtain the lessor's consent to the sublease of property, or to exclude such obligation in full.
- Because para. 2, Article 615 of the Russian Civil Code does not provide mandatory requirements for the procedure, form and terms of giving consent to the sublease of property, such consent may be reflected in the lease agreement, and the lessee does not need to obtain consent to each particular transaction.
- The legal nature of the owner's consent to the lessee's transactions for disposal of property is a unilateral transaction which does not depend on the lessee's will (para. 2, Article 154 of the Russian Civil Code).
- The lessor, acting at its own discretion, may withdraw its prior consent to the transaction by notifying the counterparty prior to the transaction and compensating it for damages caused by such withdrawal (para. 57 of Ruling of the Plenum of the Supreme Court of the Russian

² Judgment of the *Arbitrazh* Court of the Khabarovsk Region dated December 1, 2016 in Case No. A73-5337/2016.

³ Ruling of the Sixth *Arbitrazh* Court of Appeal dated March 14, 2017 No. 06AII-252/2017 in Case No. A73-5337/2016.

⁴ Ruling of the *Arbitrazh* Court of the Far Eastern District dated July 4, 2017 No. Ф03-2062/2017 in Case No. A73-5337/2016.

Federation No. 25 dated June 23, 2015). The lessee is not able to influence the lessor's unilateral right to consent to the sublease of leased property, nor restrict its right to withdraw such consent prior to the transaction.

- Because the lessee was aware of the lessor's withdrawal of its consent to transfer of the property to third parties for their use and nevertheless continued to sublease the property, such actions of the lessee are deemed a material breach of the lease agreement which entail its early termination (para. 2, Article 450, para. 3, Article 615 and para. 1, Article 619 of the Russian Civil Code).

THE RUSSIAN SUPREME COURT POSITION

The Russian Supreme Court, in its Ruling dated January 22, 2018, upheld the judgments of the court of the first instance and the court of appeal, disagreeing with the rationale for termination of the lease agreement due to material breach of its terms for the following reasons:

- The lease agreement does not stipulate that the lessor may unilaterally amend (by giving notice of withdrawal of its consent to the sublease of property) the provision regarding the lessee's right to sublease the property without further consent of the lessor.
- As the parties have agreed that the lessee may sublease the property in the lease agreement, such provision is neither in conflict with provisions of Article 615 of the Russian Civil Code (which does not prevent the parties from stipulating other rules in the agreement, and does not contain requirements for the method, procedure and form of giving the lessor's consent to transactions), nor is it a prior consent to the transaction within the meaning of para. 3, Article 157.1 of the Russian Civil Code.
- The lessor's consent to the lessee's sublease of the property stipulated by the lease agreement may not be withdrawn unilaterally. Such provision may be amended only by agreement of the parties, and the lessor was not granted the right to unilateral amendment of the contractual terms under the lease agreement.
- The lessor's unilateral amendment of the lease agreement provision regarding the possibility of sublease of property deprives the lessee of what it expected to receive upon the execution of the agreement, the purpose of which was arrangement by the lessee of office premises for their further sublease.

PRACTICAL RECOMMENDATIONS

In view of the courts' positions and the considerations discussed above, when negotiating lease agreements we recommend giving thorough consideration to the sublease of property and detailing to the maximum extent, in particular, the following issues:

- Conditions upon fulfillment of which the property may be subleased;
- The range of persons to whom the property may be subleased;

- The sort of consent granted for sublease of the property: general consent, i.e. to any transactions, or separate consent to each particular transaction;
- Procedure for provision, form and other conditions of the lessor's consent to the sublease of property;
- The procedure for amending the provision regarding the lessor's consent to the sublease of the property (including possible express prohibition of unilateral withdrawal of such consent); and
- The possibility of unilateral amendment of the agreement provision on the sublease of property.

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We will be happy to answer any questions you may have on this subject.

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