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Sanctions and International Arbitration: Challenges created by the Sanctions imposed on Russia following its Invasion of Ukraine

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Given that economic sanctions are expressly intended to interfere with international trade, it is inevitable that they create conflicts between contractual and compliance obligations, and that such conflicts may ultimately need to be resolved through international arbitration.

This article examines such conflicts and the particular challenges that the sanctions imposed on Russia following its recent invasion of Ukraine have created for international arbitration. As will be demonstrated, these sanctions will not only generate disputes, many of which may be submitted to arbitration, but also significantly complicate the process of resolution of such disputes. Given the extent of trade and investment between Russia and the western economies that have imposed sanctions on Russia, the unprecedented impact of these sanctions regimes along with the legislation that Russia has adopted to counteract the effect of foreign sanctions, these disputes and the arbitrations that may result from them may persist for years to come and could prove intractable.

Section A of this article contains an overview of the sanctions, or restrictive measures, that the United States, the European Union and the United Kingdom have imposed on Russia since its invasion of Ukraine in February 2022. Section B considers the extent to which U.S., EU, U.K. and other sanctions impact the conduct of an arbitration at its different stages, and the ability to enforce an arbitral award against a sanctioned person. It also considers the likely effect of some of the measures that Russia has implemented to counteract those sanctions on international arbitrations involving Russian parties. Section C provides some conclusions and recommendations, including on how relevant institutions such as the European Union should adapt existing sanctions regulations to counteract the effect of Russian legislation intended to undermine the international arbitration system.

1. With thanks to my colleagues Les Carnegie, Fernando Mantilla-Serrano, Thomas Lane and others who cannot be mentioned for their helpful comments. The views stated in this article are those of the author, and do not necessarily reflect those of Latham & Watkins or any of its partners, associates or clients.

A. The Sanctions imposed on Russia following its 2022 Invasion of Ukraine

Unlike United Nations sanctions, such as the comprehensive financial and trade embargo that the United Nations Security Council imposed on Iraq following its invasion of Kuwait,[2] the sanctions imposed on Russia following its invasion of Ukraine have been imposed unilaterally by certain countries pursuant to their foreign policy imperatives, albeit on an unprecedented scale and in a coordinated manner.

1. The Jurisdictional Scope of U.S., EU and U.K. Sanctions

These unilateral measures do not constitute part of international law, and the jurisdictional scope of their application depends on the legal regimes of the countries that have implemented them. Given the differences between the jurisdictional scope of U.S., EU and U.K. sanctions, and the controversies related to their perceived extra-territorial effect, it is useful to summarise how and to whom these different sanctions measures apply.

With regards to U.S. sanctions, it is first important to distinguish between so-called "primary" sanctions and "secondary" sanctions.

U.S. primary sanctions, which are generally imposed by Executive Orders issued by the U.S. President pursuant to emergency powers granted by Congress (they generally cite a number of different statutory sources[3]), are principally administered and enforced by the Office of Foreign Assets Control (OFAC), part of the U.S. Department of the Treasury. As clarified by OFAC, U.S. primary sanctions such as those imposed on Russia are binding on "U.S. persons", a term that includes all U.S. citizens and permanent resident aliens regardless of where they are located, all persons and entities within the United States (regardless of nationality), and all entities organised under U.S. law and their foreign branches.[4] In practice, U.S. primary sanctions also apply to transactions denominated in U.S. dollars that involve the participation of U.S. financial institutions, e.g., through the U.S. dollar clearing system, transactions involving U.S.-origin property, and the conduct of non-U.S. persons that cause a U.S. person to breach U.S. sanctions. As a result, U.S. primary sanctions have a broad jurisdictional reach in respect of activities involving non-U.S. persons that take place outside of the United States.

U.S. secondary sanctions, on the other hand, specifically target non-U.S. persons and have an intended extra-territorial effect. U.S. secondary sanctions are often contained in legislation, such as the Countering America's Adversaries Through Sanctions Act (CAATSA), and identify penalties that the U.S. Government may impose on non-U.S. persons that engage in certain targeted activities, the

2. See in particular U.N. Security Council resolution 661 (1990) and subsequent resolutions, including resolution 778 (1992).

3. The two main underlying congressional sources for the imposition of U.S. sanctions are the Trading with the Enemy Act, passed by Congress in 1917, and the International Economic Emergency Powers Act, adopted in 1977.

4. See Basic Information on OFAC and Sanctions, FAQ 11, available at https://home.treasury.gov/policy-issues/financial-sanctions/faqs.

most extreme being inclusion in OFAC's list of "Specially Designated Nationals" (SDNs). In the context of the Russia-related programme, secondary sanctions are found in various Executive Orders that expose non-U.S. persons to a designation on the SDN list if determined "*to have materially assisted, sponsored, or provided financial, material to*" an SDN.[5] If a non-U.S. person is added to the SDN list, that person's assets are blocked and U.S. persons are generally prohibited from dealing with them. Given the ramifications of such designation (that person would effectively be excluded from the international finance system), the available penalties under U.S. secondary sanctions are harsh.

Unlike the United States, neither the European Union nor the United Kingdom, nor other countries that have imposed sanctions on Russia, such as Canada, Australia and Japan, have adopted "secondary" sanctions with an explicit extra-territorial remit. Indeed, in respect of other U.S. sanctions regimes, such as those imposed on Cuba and Iran, the European Union, the United Kingdom and other countries have adopted blocking legislation intended to protect their nationals from the extra-territorial effect of those U.S. sanctions, which they perceive to be unlawful from the perspective of international law.[6]

However, EU and U.K. (and certain other) sanctions regimes nevertheless have an effective extra-territorial application in the sense that they apply to conduct of their own nationals that take place outside the territory of the respective countries.

Thus, EU Council Regulations (which have direct legal effect as a matter of EU law) contain standard language that the sanctions (or "restrictive measures") set out in these legal acts apply:

> "*(a) within the territory of the Union;*
> *(b) on board any aircraft or any vessel under the jurisdiction of a Member State;*
> *(c) to any person inside or outside the territory of the Union who is a national of a Member State;*
> *(d) to any legal person, entity or body, inside or outside the territory of the Union, which is incorporated or constituted under the law of a Member State;*
> *(e) to any legal person, entity or body in respect of any business done in whole or in part within the Union*."[7]

Since leaving the European Union, the United Kingdom has implemented an autonomous sanctions regime which applies to all individuals and legal entities who are within or undertake activities within the territory of the United Kingdom. All U.K. nationals and legal entities established under U.K. law, including their branches, must also comply with U.K. sanctions, irrespective of where their activities take place.

The Office of Financial Sanctions Implementation (OFSI), the U.K. financial sanctions authority, has further issued guidance that states that a U.K. jurisdictional nexus (in which case U.K. sanctions would apply) "*might be created by such things as a UK company working overseas, transactions using clearing services in the UK,*

5. See Executive Order 14024 of April 15, 2021.

6. See, for example, Council Regulation (EC) No. 2271/96, the preamble of which reads: "*Whereas by their extra-territorial application such laws, regulations and other legislative instruments violate international law …*"

7. See, for example, Article 13 of Council Regulation (EU) No 833/2014.

actions by a local subsidiary of a UK company (depending on the governance), action taking place overseas but directed from within the UK, or financial products or insurance bought on UK markets but held or used overseas."[8]

Accordingly, U.S., EU and U.K. sanctions all have an effective broad extra-territorial reach, which has important consequences in the context of an international arbitration. Irrespective of whether any of these (or other) sanctions regimes might apply to one or more of the parties to a particular dispute, they may apply as part of the law of the seat of arbitration (for example, if the seat of the arbitration is in Paris, the conduct of the arbitration will need to comply with EU sanctions). Any arbitral institution and staff members will need to comply with sanctions applicable to them by virtue of their nationality, as will counsel to either party and the individual arbitrators (a U.S. arbitrator will need to comply with U.S. sanctions, irrespective of whether U.S. primary sanctions apply to any of the parties to the dispute). Separately, sanctions laws of a particular country may arguably form part of the governing law of the arbitration (for example, if two non-EU parties have selected French law as the law applicable to a specific dispute, it may be arguable that EU sanctions should apply as part of the governing law).

Further complexity results from the potential application of U.S. secondary sanctions which, as noted above, apply to non-U.S. persons. Indeed, in a 2020 decision, the English Court of Appeal held that U.S. secondary sanctions constituted "mandatory" provisions of law that excused contractual performance by a U.K. financial institution.[9] The Court of Appeal agreed that non-payment of interest under a facilities agreement was excused "*in order to comply with a mandatory provision of law, regulation or order of any court of competent jurisdiction*." That decision turned on the language of the specific contract, but losing parties (and potentially counsel and arbitrators) may be at risk of penalties under U.S. secondary sanctions if, for example, they make a payment to an SDN in breach of relevant U.S. secondary sanctions legislation.

2. The Content of the U.S., EU and U.K. Sanctions imposed on Russia

This article does not provide a comprehensive overview of the content of the U.S., EU and U.K. sanctions regimes imposed on Russia, not least since the regimes are constantly evolving. However, its useful to explain the structure of the different regimes.

It is first relevant to clarify that U.S. sanctions regimes fall into two general categories: those that constitute a comprehensive embargo on virtually all trade and other activities with the targeted country or territory and those that are limited to certain, defined trade restrictions.

The comprehensive sanctions regimes that the United States currently has in place are those imposed on Cuba, Iran, North Korea and Syria, along with those

8. OFSI enforcement and monetary penalties for breaches of financial sanctions, Guidance, para. 3.8. Furthermore, U.K. sanctions are generally extended by Orders in Council to apply in the Channel Islands, the Isle of Man and to British Overseas Territories such as the Cayman Islands and the British Virgin Islands.

9. *Lamesa Investments Limited v Cynergy Bank Limited* [2020] EWCA Civ 821.

that target Crimea (referred to as the Crimea region of Ukraine) and the so-called People's Republics of Donetsk and Luhansk. Absent an exception under the respective sanctions regime or a general or specific licence issued by OFAC, trade and other dealings with any of these countries or territories is prohibited, assuming a U.S. jurisdictional nexus.

Aside from these comprehensive sanctions regimes, the United States maintains a number of targeted sanctions regimes or "programs." These can be divided into programmes targeting a specific country or region, such as Russia and Belarus (which are not, currently, the subject of a comprehensive U.S. trade embargo), and programmes that target a specific issue, group or activity (such as narcotics trafficking, terrorism, cyber-related activities, and global human rights).[10] The specific measures implemented pursuant to these regimes vary.

OFAC also maintains its list of SDNs, referred to above. If a person or entity is designated as an SDN (and added to the SDN list), their property is frozen or "blocked" as a matter of U.S. law, and U.S. persons are prohibited from dealing with property belonging to such persons (at least absent an exception or OFAC licence). Further, by operation of OFAC's so-called 50 percent rule, property and interests in property of entities directly or indirectly owned 50 percent or more in the aggregate by one or more SDNs are considered blocked, and it is consequently prohibited to engage in any dealing not only with SDNs, but also entities owned 50 percent or more in the aggregate by one or more SDNs.

The U.S. SDN list needs to be contrasted with other sanctions lists maintained by OFAC. Whereas all dealings with SDNs are prohibited (at least absent an exception or OFAC licence), entities listed on other lists may only be subject to certain restrictions. For example, OFAC's Sectoral Sanctions Identifications (SSI) list includes entities operating in sectors of the Russian economy that are the target of only certain "sectoral" sanctions, notably, restrictions on dealing with newly issued equity and the provision of certain types of financing.

Given the distinction between these different sanctions lists maintained by OFAC, different risks may arise in dealing with different types of U.S. sanctioned persons in the context of an arbitration. Arbitrating with an SDN may be effectively illegal assuming a U.S. jurisdictional nexus (absent an OFAC licence), whereas dealing with an entity on the SSI list may be permissible so long as no new financing is extended to that party.

While the United States has imposed country-wide or territory-wide trade embargoes on certain countries and territories, the European Union and the United Kingdom have not. Although both the European Union and the United Kingdom have imposed restrictions on certain types of trade with and investment in Iran, North Korea and Syria, along with certain other countries, including Russia and Belarus, none of them amounts to a comprehensive embargo, and neither the EU nor the U.K. have any sanctions on Cuba. Likewise, although the EU and the U.K. have imposed very broad restrictions on investment in and trade with Crimea and Sevastopol along with the non-government controlled areas of the Donetsk, Kherson, Luhansk and Zaporizhzhia oblasts of Ukraine, these restrictions do not amount to a comprehensive trade embargo.

10. The list of the different U.S. sanctions programmes is available at https://home.treasury.gov/policy-issues/financial-sanctions/sanctions-programs-and-country-information.

Similar to the U.S. SDN list, the European Union and the United Kingdom maintain consolidated lists of persons and entities subject to blocking, or so-called asset-freeze, sanctions.

These sanctions essentially provide that funds and economic resources belonging to, owned, held or controlled by any designated person are frozen, and provide that it is prohibited (absent an exception or licence from a competent sanctions authority) to make available, directly or indirectly, funds or economic resources to or for the benefit of a designated person.

Although these targeted sanctions mirror the U.S. SDN sanctions to a certain extent, they bear some differences. For example, while the OFAC 50 percent rule extends the application of U.S. sanctions to entities 50% or more owned by one or more SDNs, EU and U.K. sanctions apply to entities majority owned or controlled by a designated person. Therefore diligence must be undertaken to ascertain not only the legal owner of a counter-party in an arbitration, but also the person or persons that exercise control over that entity taking into account certain factors identified in the corresponding sanctions regime. To add further complexity to the issue, the European Commission in April 2022 issued guidance that if an entity is owned by two or more designated persons, their ownership interests should be aggregated.[11] The result is that if a company is 30% owned by one designated person and 25% by another, the company itself should be subject to asset-freeze sanctions. By contrast, the U.K. financial sanctions authority, OFSI, around the same time, clarified that "*When making an assessment on ownership and control, OFSI would not simply aggregate different designated persons' holdings in a company, unless, for example, the shares or rights are subject to a joint arrangement between the designated parties or one party controls the rights of another.*"[12]

3. The U.S., EU and U.K. Sanctions imposed on Russia

Although the United States and the European Union (which at that time included the United Kingdom) in 2014 imposed sanctions on Russia in response to its annexation of Crimea, those sanctions were, at least if considered with hindsight, relatively limited. Both the United States and the European Union imposed limited trade restrictions on Russia, particularly targeting non-conventional oil projects (i.e., deepwater, Arctic and shale). They also imposed broad trade and investment restrictions on Crimea, and designated various Ukrainian and Russian individuals and entities, in particular those associated with the steps taken to undermine the territorial integrity and sovereignty of Ukraine and misappropriating Ukrainian state funds.

The 2014 measures appear insignificant when contrasted with the unprecedented sanctions that the United States, the European Union, the United Kingdom, along with countries such as Switzerland, the European Economic Area countries (Norway, Iceland and Liechtenstein), Canada, Australia and Japan have since imposed on Russia.

11. European Commission, Asset Freeze and Prohibition to Make Funds and Economic Resources Available, Frequently Asked Questions, No. 8.

12. U.K. Finance Sanctions, General guidance for financial sanctions under the Sanctions and Anti-Money Laundering Act 2018, para. 4.1.1.

Although these sanctions regimes are broadly aligned, differences and discrepancies exist between the various regimes that have resulted in significant challenges to companies operating globally (which may be required to comply with multiple sanctions regimes) and have significantly increased the scope for disputes.

Detailing the U.S., EU and U.K. sanctions regimes and the differences between them is beyond the scope of this article. Besides their range and complexity, the different measures are constantly evolving such that a description of the measures in force at the time of writing will almost certainly be out of date by the date of publication. But the challenges that the differences between the various regimes cause are already apparent.

For example, export restrictions under one sanctions regime may apply to certain items that are not restricted by another sanctions regime, and an exception or licence granted by the competent sanctions authority in one jurisdiction will not have legal effect in another. Therefore, if a company manufactures goods in the United Kingdom and exports them to Russia from Germany, it will be subject to the U.K. and EU sanctions regimes, and even if a licence may be available in the United Kingdom, exporting from Germany to Russia may require separate authorisation or may simply be prohibited.

Similarly, the trade and investment restrictions differ between the various sanctions regimes. For example, the EU restrictions on the import of Russian-origin crude oil and petroleum products contain important exceptions which are not reflected in the equivalent U.S. and U.K. sanctions. The United States and the United Kingdom have imposed broad prohibitions on new investments in Russia, whereas the European Union's current investment prohibition is limited to investments in the energy sector. The United Kingdom has implemented broad prohibitions on dealing with securities newly issued by, or extending new credit to, persons connected with Russia (as defined in the U.K. sanctions regulations), going far beyond the equivalent restrictions contained in the EU or U.S. sanctions. The European Union has adopted a €100,000 limit on the amount of funds that Russian nationals can deposit in EU banks, whereas the United Kingdom, despite initial announcements, has not implemented any similar restriction.

Furthermore, significant discrepancies exist between the United States SDN list and the EU and U.K. lists of asset-freeze targets. Alongside the different rules and guidance regarding ownership and control and aggregation of shareholdings, these discrepancies are likely to result in disputes. For example, EU borrowers under credit facilities involving Russian lenders sanctioned by the United States and the United Kingdom, but not the EU, may nevertheless be unwilling to make repayments directly to the Russian sanctioned bank, particularly if the facility agent is in, for example, London. Another issue presenting particular challenges for western companies relates to dealings with Russian businesses in which sanctioned shareholders transferred their equity interest to close family members or local managers at around the time that they were designated. The European Commission has issued guidance that transfers of assets to avoid the effects of a possible future designation can amount to circumvention (which is prohibited under the sanctions regulations) and that, irrespective of the transfers of legal title, such assets should be frozen if there are reasonable grounds to believe that the assets "*belong to*"

or are "*controlled by*" the listed person.[13] However, the European Commission guidance is expressly stated not to be legally binding, and there is significant scope for disputes (and arbitrations) when an EU actor refuses to comply with a contractual obligation if it considers that its counterparty is controlled by an EU sanctioned person, despite assurances of the counterparty to the contrary.

B. The Impact of Sanctions and Russian Counter-Sanctions on International Arbitration

It is already apparent that the imposition of sanctions on Russia is interfering with existing contractual obligations between private actors, and that such conflicts are giving rise to disputes which may be submitted for resolution by arbitration (or litigation). However, besides the fact that international trade sanctions may be giving rise to international arbitrations, they are also impacting in a number of important respects the resolution of such disputes, whether by international arbitration or court litigation.

1. The Impact of Sanctions on the Ability to Participate in an International Arbitration

If a party to an arbitration is designated under a specific sanctions regime, one immediate issue is whether the counterparty (and its counsel) can participate in the arbitration, whether individuals of specific nationalities can preside over the arbitration as tribunal members, and whether particular arbitral institutions and their staff members are subject to any constraints to administer an arbitration involving such persons (including by acceptance of an advance on costs from a sanctioned party).

The extent to which parties, counsel, arbitrators or arbitral institutions may be constrained from participating in an arbitration will depend on the applicable sanctions regime. For example, under U.S. sanctions it may be prohibited for U.S. persons to participate in an arbitration outside the United States involving sanctioned persons or sanctioned countries without a licence from OFAC. Under EU or U.K. sanctions, on the other hand, participation in an arbitration involving EU or U.K. asset-freeze targets may be permissible, but if it is necessary to access funds belonging to a sanctioned person, including to pay counsel for their fees,[14] a licence from the competent sanctions authority may be required.[15]

At the time of writing, U.S., EU and U.K. sanctions do not prohibit their respective nationals (or other persons to which the respective sanctions regimes

13. European Commission, Asset Freeze and Prohibition to Make Funds and Economic Resources Available, Frequently Asked Questions, Nos. 5 and 25.

14. U.K. and the EU sanctions regulations generally provide for the possibility to release frozen funds to pay for reasonable professional fees for legal services and associated expenses. See, for example, Article 4.1(b) of Council Regulation (EU) No 269/2014 and Schedule 5, Part 1, Regulation 3 of the Russia (Sanctions) (EU Exit) Regulations 2019.

15. OFSI has issued a general licence permitting the receipt of payments from designated persons for legal services subject to certain conditions (INT/2022/2252300) and a separate licence permitting payment of funds to the LCIA to cover arbitration costs (INT/2022/1552576).

apply) from representing Russian clients in arbitration proceedings. The EU has implemented a prohibition on providing "*legal advisory services*" to the Government of Russia or legal persons, entities or bodies established in Russia.[16] However, the recital to the relevant amending regulation clarifies that this prohibition does not apply to representing clients in arbitration proceedings.[17] Article 5n.5 also states that this prohibition does not apply to provision of services that are "*strictly necessary for the exercise of the right of defence in judicial proceedings and the right to an effective legal remedy*," and Article 5n.6 provides that it "*shall not apply to the provision of services which are strictly necessary to ensure access to judicial, administrative or arbitral proceedings in a Member State, or as well as for the recognition or enforcement of a judgment or an arbitration award rendered in a Member State, provided that such provision of services is consistent with the objectives of this Regulation and of Council Regulation (EU) No 269/2014*". Although the U.K. has announced that it intends to implement a prohibition on the provision of legal services in its Russia sanctions regime, neither it nor the United States has yet done so.

The breadth of certain sanctions provisions may also present particular challenges to the conduct of arbitrations. For example, Article 5aa of Council Regulation (EU) No 833/2014 provides that it is prohibited "*directly or indirectly engage in any transaction with*" certain publicly-owned Russian entities listed in Annex XIX and their subsidiaries. This extremely broadly worded provision raised immediate concerns as to whether arbitrations may be conducted in the EU involving any such listed entities. Faced with this uncertainty, a number of European arbitral institutions contacted the European Commission to obtain clarification on this point.[18] In response, the European Union amended Article 5aa to exempt from the prohibition "*transactions which are strictly necessary to ensure access to judicial, administrative or arbitral proceedings in a Member State, as well as for the recognition or enforcement of a judgment or an arbitration award rendered in a Member State, if such transactions are consistent with the objectives of this Regulation and Regulation (EU) No 269/2014*."[19]

However, despite this clarification and the fact that sanctions authorities are expressly authorised to approve the payment of legal fees by sanctioned persons in arbitration and other legal proceedings, it has been widely reported that many U.S., EU and U.K. law firms have adopted internal policies not to provide legal services to Russian clients, including State-owned entities and sanctioned persons. This state of affairs has raised concerns among Russian parties as to whether they can fairly access justice in international arbitration proceedings conducted in the United States and western Europe. This general concern has been invoked to justify

16. See Article 5n.2 of Council Regulation (EU) No 833/2014 (as amended).

17. See Council Regulation (EU) 2022/1904, Recital (19), which clarifies that this prohibition applies to the provision of legal advisary services in non-contentious matters, and that "*'Legal advisory services' does not include any representation, advice, preparation of documents or verification of documents in the context of legal representation services, namely in matters or proceedings before administrative agencies, courts or other duly constituted official tribunals, or in arbitral or mediation proceedings*."

18. See Joint Statement of SCC, VIAC, FAI, DIS, CAM and Swiss Arbitration Centre dated 26 July 2022, available at https://sccinstitute.com/media/1843377/joint-statement-7th-sanctions-package-26-july-2022_final.pdf

19. See Article 5aa.3(g) of Council Regulation 833/2014.

the adoption of Russian legislation intended to counteract any potential prejudice to Russian sanctioned persons compelled to engage in international arbitration proceedings outside of Russia.

2. The Impact of Sanctions on the Resolution of Disputes submitted to International Arbitration

Irrespective of the ability of specific persons to participate in an arbitration involving sanctioned persons, sanctions may impact the resolution of a dispute submitted to international arbitration in a number of different respects.

As noted above, disputes submitted to arbitration may be the result of a conflict between performance obligations under a contract and compliance obligations incumbent on that party. For example, if one of the parties to a contract has been designated as a target of sanctions under a specific sanctions regime, the non-sanctioned counterparty may consider that it is excused of performance of its contractual obligations, potentially by operation of contractual terms, such as force majeure provisions, or at least by operation of applicable sanctions laws.

In this regard, EU sanctions regulations contain standard provisions intended to protect EU and other persons from liability on account of steps they have taken to comply with EU sanctions. A typical "no claims" provision is contained in Article 11.1 of Council Regulation (EU) No 833/2014 as follows:

> "*1. No claims in connection with any contract or transaction the performance of which has been affected, directly or indirectly, in whole or in part, by the measures imposed under this Regulation, including claims for indemnity or any other claim of this type, such as a claim for compensation or a claim under a guarantee, notably a claim for extension or payment of a bond, guarantee or indemnity, particularly a financial guarantee or financial indemnity, of whatever form, shall be satisfied, if they are made by:*
>
> *(a) legal persons, entities or bodies listed in the Annexes to this Regulation or legal persons, entities or bodies established outside the Union whose proprietary rights are directly or indirectly owned for more than 50% by them;*
> *(b) any other Russian person, entity or body;*
> *(c) any person, entity or body acting through or on behalf of one of the persons, entities or bodies referred to in points (a) or (b) of this paragraph*."

Such "no claims" provisions have to date been subject to relatively little judicial scrutiny.

The judgment of the English Court of Appeal in *Ministry of Defence & Support for Armed Forces of the Islamic Republic of Iran v International Military Services Ltd*[20] is one of the leading decisions regarding such a clause.[21] That case concerned

20. *Ministry of Defence & Support for Armed Forces of the Islamic Republic of Iran v International Military Services Ltd* [2020] EWCA Civ 145.

21. An earlier example is the decision of the Quebec Court of Appeal related to Council Regulation (EC) No 3275/93, which prohibited the satisfying of claims with regard to contracts and transactions the performance of which was affected by the U.N. sanctions on Libya. The Quebec Court of Appeal considered Air France's reliance on a slightly more broadly worded "no claims" provision to justify its refusal to appoint an arbitrator in an arbitration commenced by Libyan Arab

whether IMS Ltd, a company owned by the U.K. Ministry of Defence, was liable to pay interest on an International Chamber of Commerce (ICC) award rendered in favour of MODSAF, the Iranian Ministry of Defence. MODSAF had been designated as an asset-freeze target during the period in which it was unable to satisfy the ICC award due to EU sanctions in light of the (similarly worded) "no claims" provision contained in Council Regulation (EU) No 267/2012 (containing the EU Iran trade sanctions).

The Court of Appeal confirmed that the purpose of the provision was to "*protect parties against claims being brought against them by virtue of their non-performance of a contract or transaction that was caused by the sanctions*."[22] The court held that MODSAF's application for a judgment to be entered in its favour was a "*claim*" "*in connection with any contract or transaction*" (being the contracts underlying the arbitral award), and that the application was "*for the … enforcement … of … an arbitration award*," thereby falling within the scope of the "no claims" provision.[23] As a result, the Court of Appeal denied MODSAF's claim for interest on the award during the period in which IMS was unable to honour it due to EU sanctions.

The Court of Appeal relied in part on judgment of the General Court of the European Union in *PAO Rosneft Oil Company v Council*.[24] The General Court in that case held that the "no claims" provision in Council Regulation (EU) No 833/2014 did not constitute a disproportionate interference in Rosneft's fundamental rights or to its access to the courts under Article 6 of the European Convention on Human Rights, given that Rosneft was able to bring proceedings before the domestic courts of an EU Member State and the General Court to contest the measures in question.[25]

Separate from the "no claims" provisions found in EU sanctions regulations, EU asset-freeze sanctions regulations generally contain a "no liability" provision such as Article 10.1 of Council Regulation (EU) No 269/269, which reads:

> "*The freezing of funds and economic resources or the refusal to make funds or economic resources available, carried out in good faith on the basis that such action is in accordance with this Regulation, shall not give rise to liability of any kind on the part of the natural or legal person or entity or body implementing it, or its directors or employees, unless it is proved that the funds and economic resources were frozen or withheld as a result of negligence*."

Accordingly, an EU person who refuses to make funds available to a Russian sanctioned person should not face any liability as a matter of EU law unless such refusal can be demonstrated to be negligent. Although this provision does not shield EU persons from the risk of claims, it affords them a level of legal protection in respect of steps they have taken to comply with EU sanctions.

Airlines. The arbitral tribunal rejected Air France's position, and the Quebec Court of Appeal's decision focussed on the fact that the underlying U.N. Security Council resolution did not prohibit Air France from appointing an arbitrator. *Air France v. Libyan Arab Airlines*, Quebec Court of Appeal, 31 March 2008.

22. Para. 40.
23. Paras. 49 and 57.
24. *Case T-715/14 PAO Rosneft Oil Company v Council* EU:T:2018:544
25. Paras. 207-212.

The United Kingdom has included a "no liability" provision in the Sanctions and Anti-Money Laundering Act 2018 (the umbrella legislation for the autonomous sanctions regulations that the United Kingdom adopted after its departure from the European Union).[26] However, it has not included a "no claims" provision that mirrors the one found in EU sanctions regulations (and none exists in U.S. sanctions regulations). Accordingly, it is a characteristic of EU sanctions law that Russian parties appear to be precluded as a matter of EU sanctions law from bringing claims against EU persons in connection with contracts or transactions whose performance has been affected, directly or indirectly, by measures contained in EU sanctions.

3. The Impact of Russian Counter-Sanctions on the Resolution of Disputes submitted to International Arbitration

A further layer of complexity to the resolution of sanctions-related disputes by courts and tribunals is caused by legislation that Russia has adopted in order to counteract the impact of sanctions imposed by the United States, the European Union, the United Kingdom and other so-called "unfriendly" countries on Russia since 2014.

Of particular relevance for international arbitration are the amendments to the Russian Commercial Procedure Code (also referred to the Russian Arbitrazh Procedure Code) introduced through Federal Law No. 171-FZ in June 2020.[27] These rules provide that the Russian state courts may exercise exclusive jurisdiction over disputes: (a) involving Russian citizens, Russian legal entities or certain foreign legal entities subject to foreign sanctions; and (b) between a Russian or foreign person and another Russian or foreign person if the dispute arose from foreign sanctions imposed on Russian citizens or legal entities, including where the parties had agreed to dispute resolution before non-Russian courts or arbitration outside of Russia but such agreement is deemed to be incapable of being performed due the fact that one party is subject to sanctions and consequently hindered from accessing justice.

In such circumstances, the affected Russian party (or foreign party, e.g., a non-Russian subsidiary, affected by the sanctions) is entitled to apply to a Russian court on an *ex parte* basis for the Russian court to assume jurisdiction and to issue an anti-suit injunction. An injunction could be issued to prevent the counterparty not only from initiating court or arbitration proceedings outside Russia, but also from continuing with proceedings that had already commenced. Furthermore, if the counterparty proceeds with the non-Russian litigation or arbitration, the Russian court may award the damages against it.

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26. See Section 44(2) of the Sanctions and Anti-Money Laundering Act 2018: "*A person is not liable to any civil proceedings to which that person would, in the absence of this section, have been liable in respect of the act.*" It is unclear in this context whether the term "civil proceedings" would include arbitration proceedings

27. Federal Law dated 8 June 2020 (effective as of 19 June 2020) No. 171-FZ "*On Amendments to the Arbitration Procedure Code of the Russian Federation for the protection of the rights of individuals and legal entities in connection with restrictive measures imposed by a foreign state, state association and (or) union and (or) state (international) institution of a foreign state or state association and (or) union*".

Russian parties have successfully resorted to these procedural rights,[28] and the Russian courts have to date interpreted these provisions broadly. For example, Russian courts have not required that a Russian sanctioned party needs to demonstrate the effect of sanctions on its rights; the mere imposition of sanctions being deemed sufficient to demonstrate the sanctioned person stands no prospect of accessing justice in a fair trial.[29]

This legislation undoubtedly represents a major challenge to companies involved in disputes with Russian (or Russian-owned) counterparties linked to the imposition of sanctions, and which are considering resorting to a contractually agreed dispute resolution mechanism to recover damages. Indeed, these amendments to the Russian Commercial Procedure Code threaten to undermine the fabric of the international arbitration system in respect of disputes with persons that are the target of western sanctions imposed on Russia. Even though an international arbitral tribunal might involve the doctrine of competence-competence to assume jurisdiction, the non-Russian party would nevertheless face the complication of parallel court proceedings in Russia and a potential damages claim before a Russian court, which would at the very least likely frustrate any attempt to enforce an eventual award in Russia.

More legislation has been tabled before the Russian parliament that Russian persons could weaponise in disputes with western counterparties. For example, Bill No. 25200-8, which was due to be considered by the lower chamber of the Duma in March 2022, would allow Russian sanctioned persons to bring claims against foreign entities that had failed to perform contractual obligations due to sanctions, along with entities that were considered to have promoted the imposition of sanctions or to have unjustly benefited from sanctions. Another bill (No. 141547-8), which was introduced in June 2022, provides that the Russian commercial courts would have an exclusive jurisdiction over "*cases involving foreign persons registered in a foreign state or territory that has conducted unfriendly acts towards the Russian Federation, Russian legal entities or individuals*." Whether these bills will ever be enacted, and if they are, whether they will be subject to further amendments, is unclear. But the Russian State clearly intends to frustrate the operation of international arbitration involving Russian parties and counterparties from the United States, the European Union, the United Kingdom and other so-called "unfriendly" countries.

4. The Impact of Sanctions on the Ability to Honour or Enforce Arbitral Awards

Even if a party prevails in an international arbitration involving a Russian sanctioned party, and irrespective of the impact of the Russian legislation described

28. For example, Decision of the Arbitrazh Court of the City of Moscow (Case No. A40-51964/22-3-398) dated 17 June 2022, in which the Arbitrazh Court issued an injunction seeking to enjoin Patentes Talgo (a Spanish company) from initiating an ICC arbitration against JSC Federal Passenger Company, despite the fact that the parties had agreed (in a Russian law governed contract) that disputes should be resolved by ICC arbitration with seat in Paris. Patentes Talgo is currently appealing this decision.

29. Decision of the Economic Collegium of the Supreme Court of the Russian Federation No. 309-ES21-6955 (Case No. A60-36897/2020) dated 21 September 2021.

above, specific problems may arise when attempting to obtain satisfaction, including at the stage of enforcement of an arbitral award.

Sanctions regulations often provide for the possibility of obtaining a licence from the competent sanctions authority to secure payments from a sanctioned person's frozen or blocked account. However, the relevant regulations are inconsistent and contain important *lacunae*.

For example, Article 5.1(a) of Council Regulation (EU) No 269/2014 (pursuant to which the EU has designated, amongst others, a number of prominent Russian 'oligarchs' and financial institutions) provides that the competent authorities of the relevant EU Member State may authorise the release of frozen funds belonging to a sanctioned person subject to various conditions. Such conditions include that the funds are "*are subject to an arbitral decision rendered prior to the date on which the [sanctioned person was designated] or of a judicial or administrative decision rendered in the Union, or a judicial decision enforceable in the Member State concerned, prior to or after that date*."

This provision distinguishes between arbitral decisions (in respect of which funds may be released only if the decision pre-dated the designation of the sanctioned person) and court decisions (in which case funds may be released if a court decision was obtained before or after the date of designation), apparently placing arbitration (perceived to be a private dispute resolution mechanism, and potentially open to abuse) at a disadvantage to court litigation.

The U.K. Russia Sanctions Regulations, on the other hand, make no such distinction, but only provide for the possibility of obtaining a licence from OFSI to use frozen funds to satisfy judicial or arbitral decisions made before the sanctioned person was designated.[30]

Separately, Article 6(1) of Council Regulation (EU) No 269/2014 provides that:

> "*By way of derogation from Article 2 and provided that a payment by a natural or legal person, entity or body listed in Annex I is due under a contract or agreement that was concluded by, or under an obligation that arose for the natural or legal person, entity or body concerned, before the date on which that natural or legal person, entity or body was included in Annex I, the competent authorities of the Member States may authorise, under such conditions as they deem appropriate, the release of certain frozen funds or economic resources, provided that the competent authority concerned has determined that:*
>
> *(a) the funds or economic resources shall be used for a payment by a natural or legal person, entity or body listed in Annex I; and*
> *(b) the payment is not in breach of Article 2(2)*."

Accordingly, under the EU regime it may nevertheless be possible to secure a licence for the release of frozen funds belonging to a sanctioned person if the payment was due to a contract or obligation that pre-dated the date of designation of the sanctioned person.

By contrast, the U.K. sanctions are more limited, and provide that a licence may only be obtained "*To enable, by the use of a designated person's frozen funds or economic resources, the satisfaction of an obligation of that person (whether*

30. Schedule 5, Part 1, Regulation 6 of the Russia (Sanctions) (EU Exit) Regulations 2019.

arising under a contract, other agreement or otherwise), provided that—(a)the obligation arose before the date on which the person became a designated person, and (b) no payments are made to another designated person, whether directly or indirectly."[31]

Under the U.S. rules, OFAC may not be so constrained, but the ability to secure access to frozen funds would nevertheless be subject to the discretion of OFAC and its willingness to grant a licence in specific circumstances.[32]

C. Conclusions

The U.S., EU, U.K. and other sanctions that have been imposed on Russia following its invasion of Ukraine have undoubtedly caused significant business disruption, and the scope for resulting arbitrations is obvious. However, the same sanctions rules that have resulted in such disputes are clearly impacting the ability of non-Russian parties to resolve those disputes successfully in accordance with agreed dispute resolution mechanisms, and parties to such disputes will in many cases need to obtain authorisation from the competent sanctions authorities to ensure that international arbitrations can proceed fairly and efficiently. Moreover, both western sanctions regulations and Russian counter-sanctions will likely significantly impact the ability of successful litigants to enforce arbitral awards against Russian counterparties.

The governments responsible for implementing these sanctions need to be aware of the challenges, including the likely prejudice that parties to disputes with Russian entities will face in attempting to resolve those disputes in accordance with international arbitration mechanisms that are designed to operate in a fair and neutral manner. Governments and sanctions authorities furthermore need to take note of the steps that the Russian parliament and the Russian courts are taking to undermine the system of international arbitration, and should react accordingly. For example, western governments and rule-makers should ensure that both western and Russian parties can participate freely and fairly in international arbitration proceedings, and put in place protective measures where Russian courts may attempt to frustrate the operation of international arbitration proceedings or award damages against western actors that have resorted to international arbitration. Furthermore, if Russian legislation has effectively undermined the ability to the enforce awards against Russian parties in Russia, governments should consider amending sanctions regulations to facilitate the enforcement of court judgments and arbitral awards, including against frozen assets located outside of Russia.

31. Schedule 5, Part 1, Regulation 8 of the Russia (Sanctions) (EU Exit) Regulations 2019.

32. In the United States it is generally prohibited to attach blocked funds. Most sanctions programmes contain provisions along the following lines: "*Unless licensed pursuant to this part, any attachment, judgment, decree, lien, execution, garnishment, or other judicial process is null and void with respect to any property or interest in property blocked pursuant…*" See https://www.ecfr.gov/current/title-31/subtitle-B/chapter-V/part-587.

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