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The potential impact of the EU sanctions against Russia on international arbitration administered by EU-based institutions

A lot has been said recently regarding the potential impact of the European Union ("EU") sanctions on arbitrations involving Russian parties administered by EU-based arbitration institutions. The purpose of this article is to offer a practical explanation of these sanctions and their effect, if any, upon the administration of international arbitration cases by arbitral institutions based in the EU.

1. Background

Since March 2014, the EU has imposed an array of restrictive measures targeting a number of Russian individuals and organizations. These were in addition to other, more far-reaching measures which the EU had taken in respect of, for example, Iran and Libya. Subsequently, economic sanctions have been introduced, covering sectorial cooperation and exchanges with Russia through trade bans and export/import embargoes in the financial, oil-drilling and defense sectors. Similar sanctions apply to individuals and entities in Crimea.

The relevant EU decisions and regulations contain mandatory norms applicable to specific individuals, organizations and sectors, which are identified in official lists published on the EU's website.[1]

[1] http://europa.eu/newsroom/highlights/special-coverage/eu_sanctions/index_en.htm#3

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It is perhaps not surprising then that a debate on the sanctions' effect, if any, on the work of EU-based arbitral institutions has emerged in Russia, not least given the preference of Russian parties for certain EU-based institutions and/or EU jurisdictions' national laws. However, in addition to questions regarding the intended scope of the sanctions, the current debate often includes politicized arguments, many of which appear misconstrued and/or biased against EU-based arbitral institutions. The purpose of this note is to address these issues and to clarify the impact of sanctions on the day-to-day-activities of international arbitral institutions within the EU.

Some European institutions have a steady and significant caseload involving Russian and CIS parties. Others have even seen a substantial increase in the number of cases involving such parties. In any event, the Russian sanctions – while they may result in some additional administrative steps – do not preclude parties from referring their disputes to arbitration at an EU-based institution. As such, it is very much business as usual for both the institutions and the parties.

2. International trade and arbitration from a historical perspective

History teaches us that trade and commercial relations will develop regardless of political system, priorities or even political conflict. In this context, it may be worth noting that the preference of Russian parties to use certain Western institutions originates from the times of the Cold War, which was an era of trade embargoes and general hostility between Western and Soviet blocs. This was the context in which the neutral, impartial and independent decision-making of East-West disputes by means of international arbitration developed.

Thus, nations will always trade, and nations will always have commercial relationships. Equally, States have been in agreement for a very long time that international trade and

international commercial relations need predictable rules of law, including efficient mechanisms for dispute resolution.

As we assess the current situation, it is worthwhile to reflect on the world as it was when States negotiated and agreed to some of the most relevant common legal instruments for international arbitration, for example the 1958 Convention on Recognition and Enforcement of Foreign Arbitral Awards, and the 1976 UNCITRAL Arbitration Rules. In 1958 and 1976 borders were quite different, not to mention political systems. But this did not prevent a constructive approach in providing access to justice in international trade.

In fact, from a review of the *travaux préparatoires* of these instruments, it may be noted that one of the objectives of the negotiations was to enable parties from "*different economic systems*" to find a common ground for their international relations, and that the new legislation "*would be a constructive step towards facilitating international trade, and ultimately towards higher standards of living and so towards general peace and prosperity*." These are powerful words, and, we believe, are still valid and relevant. This is particularly so when one considers that while States during this time disagreed on a number of policy and geopolitical issues, in defining the rules of the game for international arbitration, States were able to find common ground. The underlying values which States agreed upon then still matter, particularly in times of political conflict, and are reflected in certain provisions of the EU sanctions regulations. For example, an exemption from the freezing of funds can be obtained for "funds intended exclusively for payment of reasonable professional fees or reimbursement of incurred expenses *associated with the provision of legal services"*.[2]

3. The sanctions do not explicitly target the arbitral procedure

All arbitral institutions based in EU states, including SCC, LCIA and ICC, are subject to EU law. They are required to observe EU sanctions regulations, which often complement, or are intended to operate in tandem with, US (and UN) sanctions. These sanctions do not result in

[2] See article 4 of the EU Regulation 269/2014

a substantial change in the administration of arbitral proceedings. Arbitral proceedings involving EU sanctions are subject to internal compliance mechanisms specific to arbitral institutions. The institutions must ensure therefore that they have systems in place, which are sanctions compliant and which are acceptable to both the regulatory authorities charged with the administration of the sanctions regime and which the banks which handle the deposit moneys lodged with the institutions likewise find acceptable. It is important to note, however, that the EU sanctions implemented against Russian interests have targeted a limited and defined number of entities and individuals and are of a less sweeping and general nature than sanctions introduced against other states and their nationals.

In practical terms, however, in the case of Russian parties, there is a variety of situations relating to *procedure* where the sanctions could come into play. One is where a designated party appears as or is a controlling entity, i.e. the ultimate beneficial owner, of a party in one of our cases. A second is where a party to one of our cases is itself an entity trading in dual-use goods and technology for military use in Russia or for any military end-user in Russia. In such circumstances, the transfer of funds could be affected by the regulations on freezing of assets and the financial sanctions targeting certain sectors of the Russian economy. These are, however, situations that can be addressed by applying for an exemption under the regulations.

The asset-freezing restrictions might thus require additional administration on the part of the designated individuals and entities, the arbitral institutions and arbitrators. As pointed out above, this designation is a very limited list. In essence, prior to filing for arbitration the designated company or individual will need to obtain an exemption from the freezing of funds by filing a request with the relevant authority. Practical information and contact details for filing an application is available from our respective institutions.

There may be cases where sanctions have an effect on the *substance* of disputes. In such cases, the dispute itself will be affected by the sanction, i.e. from the perspective of the arbitral institution, the sanction will bite, irrespective of where the arbitration is seated,

which EU arbitral institution is administering it, the law(s) applicable to it, and where any award is ultimately sought to be enforced. As such, moving the seat of these arbitrations outside of the EU will not make any difference, if the dispute is subject to the sanctions regime.

4. Addressing some of the most common questions

In the wake of the political debate surrounding the implementation of the sanctions, a number of misconceptions have surfaced regarding the impact and applicability of the Russian sanctions. Below, we address some of the most principal issues.

- The EU sanctions apply to a limited number of persons and entities

The EU Regulations apply to a limited number of persons and entities. The sanctions do not impose a general prohibition on trade with Russian parties. Indeed, the overwhelming majority of Russian businesses and investors are not subject to any EU restrictions.

- Parties of any nationality are not prevented from referring their disputes to European institutions

Arbitral institutions maintain a strict neutrality vis-à-vis all parties, irrespective of their nationalities. Subject to compliance measures that arbitral institutions are required to implement in a case, Russian parties will not be treated differently from other parties, and Russian parties are not prevented from agreeing to arbitration under any of the of Rules or in any venue within the European Union including Paris, London and Stockholm.

- The arbitral procedure remains the same

The arbitration procedure in Europe continues to be open for all parties, irrespective of their nationalities. In this respect, nothing has changed. With the exception of compliance measures. The EU sanctions do not affect the arbitration procedure as such.

- Some administrative measures have been added

In practice, the EU Regulations and their implementation by national authorities have added a limited number of administrative steps in the case management process. To this end, additional information regarding parties' ownership or control structure may be needed at any time of the proceedings. For example, when a request for arbitration is filed, parties and related entities will be checked against a list of sanctioned individuals and entities. If the scope of the sanctions changes, institutions will take the relevant necessary steps in relation to pending cases.

- A designated party can still file a request for arbitration

A person or entity designated by the EU Regulations is not *per se* prevented from filing a request for arbitration with the ICC, LCIA or SCC.

Before so doing, however, the designated person or entity is advised to inform the institution of the dispute prior to the request for arbitration. This is to enable the institutions to discuss with the parties of any additional administrative requirement that needs to be fulfilled either by the parties or the institution, for example filing an application with the relevant national authorities for an exemption under the sanction regulation.

The freezing of funds under the sanctions regulations can be exempted for "*funds intended exclusively for payment of reasonable professional fees or reimbursement of incurred expenses associated with the provision of legal services.*"

5. Summary

The sanctions do not impose a general prohibition for Russian parties to seek arbitration before European arbitral institutions, and Russian parties are not treated differently from other parties.

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The integrity of the process of our respective institutions remains the same, as does the impartiality and independence of the procedure. We have put in place procedures to address the sanctions and are engaging with relevant public authorities to facilitate an efficient procedure should exemptions under the regulations be required. This is a responsibility that arbitral institutions share with parties, and their counsel.

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