CHAPTER 2

Paving the Way for Justice: Arbitration and EU Sanctions Against Russia

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§2.01 INTRODUCTION

Prior to 2022, the European Union's sanctions against Russia targeted a limited number of individuals and entities, and had limited effect on the day-to-day administration of arbitrations for most arbitrators and European arbitral institutions. However, the legal landscape in Europe experienced a seismic shift soon after the Russian invasion of Ukraine in February 2022. Instant termination of direct investments and international trade with Russia, coupled with the rapid expansion of the list of individuals and entities subject to sanctions, created a new legal reality with profound implications for international arbitration.

Sanctions pose a critical dilemma for the regulator of effectively reconciling the core principles of access to justice, the right to efficient remedy, and the right to legal advice with the overarching objectives of sanctions. Arbitration, the sole effective legal remedy within the realm of international trade, currently finds itself in a precarious position. On the one hand, judicial proceedings and the arbitral process are exempted from sanctions. On the other hand, as demonstrated below, the arbitral process is not entirely treated equal to judicial proceedings.

This chapter has two objectives. First, it offers a concise and practical analysis of how EU sanctions against Russia impact arbitral institutions and arbitrators located within the EU. At the time of writing, in early summer 2023, sanctions continue to expand, with the EU currently preparing its eleventh sanction package. Consequently, new effects may emerge in the near future. Nevertheless, we assess the existing regulations and each relevant provision in order to aid arbitral institutions, arbitrators, and parties in navigating the complexities of the EU sanction regime.

Second, the recommendations for necessary improvements outlined in this chapter may serve as industry feedback to the EU regulator. We hope that by providing

an understanding of the actions required, we can ensure that sanctions neither hinder the administration of justice by arbitrators and arbitral institutions nor undermine the rule of law.

§2.02 THE SCOPE OF THE EU SANCTIONS

The EU sanctions against Russia were implemented in 2014 in response to Russia's destabilizing of the situation in Ukraine and annexation of Crimea. These sanctions were primarily established through two key EU Council Regulations. The first, Council Regulation (EU) No. 269/2014 dated 17 March 2014, outlined a list of individuals and entities subject to financial sanctions, including measures such as asset freeze and restrictions on financial transactions with them. The second, Council Regulation (EU) No. 833/2014 dated 31 July 2014, introduced sectoral sanctions that imposed limitations on the export of goods and technologies in the defence and oil sectors. Additionally, it restricted certain Russian financial institutions' access to the EU capital market.

The two regulations 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.[1]

In broad terms, EU sanctions are primarily intended to be enforced within the territory of the EU and are applicable to EU nationals. However, it is important to note that EU citizens are personally obligated to adhere to these sanctions, even if they reside or work outside the EU.[2]

Therefore, the EU sanctions regime may come into play in arbitral proceedings through several different avenues, depending on the actors and the circumstances in the arbitration:

- Legal counsels and arbitrators who are nationals of a Member State must comply with the EU sanction regime when providing legal services.
- EU-based arbitral institutions must adhere to the sanction regulations, including screening the parties against sanction lists when processing advances on costs.
- Parties incorporated or domiciled in the EU must comply with the sanctions regulations when conducting business, including resolving their disputes, with Russian parties.
- EU sanctions also apply if the disputed contract is governed by the law of a Member State or has an EU nexus, i.e., concerns 'business done in whole or in part within the Union'.

1. Article 17 of Council Regulation (EU) No. 2014/269 of 17 March 2014 https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0833 and Article 13 of Council Regulation (EU) No. 2014/833 of 31 July 2014 (accessed June 2023).
2. Consolidated FAQs on the implementation of Council Regulation No. 833/2014 and Council Regulation No. 269/2014, Question 35 (accessed June 2023).

– Arbitrations *seated* in the EU must also be conducted with due regard to EU sanctions regulations for the arbitral award to be valid under the *lex arbitri*.

The EU sanctions regulations provide for certain exceptions. These exceptions come in the form of *derogations* or *exemptions*. Derogations allow for seeking the authorization of a national competent authority for making particular actions or transactions under those conditions deemed appropriate by the authority.[3] Decisions on derogations are subject to the administrative procedures of each respective country, have a limited duration, and can be challenged in national administrative courts.

Exemptions, on the other hand, carve out specific transactions and services from the general prohibitions imposed by the sanction regulations. However, it is important to note that although certain services and transactions are exempt from sanctions, it does not automatically follow that *payment* for those services can be made without prior authorization from the competent authority, for instance, if payment is due from a listed person or entity.

Due to its particular nature, legal services are dealt with specifically in the framework and are allowed under certain conditions. Technically, this is achieved through the use of exemptions and derogations incorporated in regulations 269/2014 and 833/2014.

§2.03 THE LEGAL AND PRACTICAL EFFECTS OF COUNCIL REGULATION (EU) NO. 269/2014 ON ARBITRATION

The provisions of 269/2014 that are particularly relevant for arbitration include:

– Article 2 (freeze of assets);
– Article 4.1.(b) (derogation related to legal services);
– Article 5.1 (derogation related to claims arising out of arbitral and judicial decisions);
– Article 7 (payments due under arbitral decisions for the benefit of the listed parties);
– Article 8 (reporting obligation); and
– Article 11 ('no claims' provision).

[A] Article 2: The Freeze of Assets

Article 2 states:

> 1. All funds and economic resources belonging to, owned, held or controlled by any natural or legal persons, entities or bodies, or natural or legal persons, entities or bodies associated with them, as listed in Annex I, shall be frozen.

3. The list of national competent authorities is provided in Annex II to the Regulation 2014/269 and in Annex I to the Regulation 2014/833.

> 2. No funds or economic resources shall be made available, directly or indirectly, to or for the benefit of natural or legal persons, entities or bodies, or natural or legal persons, entities or bodies associated with them, as listed in Annex I.

Article 2 imposes an obligation on the recipient of funds to conduct thorough checks on the paying party in order to establish whether the party is subject to sanctions. The scope of the obligation is broad and involves conducting extensive sanctions controls of the majority shareholders/owners, beneficial owners, and controlling entities or individuals. In arbitral proceedings, institutions and ad hoc tribunals typically handle deposits provided by parties in advance or during the proceedings. In cases where the party receives funding, the same level of scrutiny should be applied also to the funder.

In practice, the aforementioned provisions necessitate that arbitral institutions establish due diligence procedures concerning sanctions control, regardless of whether they handle cases involving Russian parties or not. As there is no rule book dictating how to design the framework for compliance with the sanctions regulations, it is up to each institution to design one. An obvious first step is to screen parties against the sanctions lists. Circumstances which may merit further investigation include situations where a party is incorporated in a country targeted by the EU sanction programmes, such as Russia and Belarus. Additionally, parties registered in offshore jurisdictions or in jurisdictions deemed high-risk or subject to increased monitoring by the Financial Action Task Force (FATF)[4] indicate an elevated risk for sanctions-related implications. Compliance with the sanctions framework therefore may require further investigation of the parties involved, such as requesting the parties to disclose their ownership structure and beneficial owners. It is helpful if the arbitration rules of the institution empower it to compel the parties to provide such information.

Further guidance is provided by the European Commission in its official frequently asked questions (FAQ) document.[5] It recommends for instance screening beneficiaries of funds against sanctions lists and conducting investigations into adverse media reports. The European Commission further suggests conducting internet searches to determine whether the party, even if not officially designated, may be under the control of a listed person or entity. The criteria for evaluating whether a legal entity is controlled by another person or entity can be found in the EU Best Practices for the effective implementation of restrictive measures.[6] These criteria include:

> (a) having the right or exercising the power to appoint or remove a majority of the members of the administrative, management or supervisory body of such legal person or entity;

4. FATF's lists are found here: https://www.fatf-gafi.org/en/the-fatf/what-we-do.html.
5. Commission consolidated FAQs on the implementation of Council Regulation No. 833/2014 and Council Regulation No. 269/2014, Chapter 2 'Circumvention and Due Diligence' https://finance.ec.europa.eu/system/files/2023-05/faqs-sanctions-russia-consolidated_en_0.pdf (accessed June 2023).
6. EU Best Practices for the effective implementation of restrictive measures, §62 https://data.consilium.europa.eu/doc/document/ST-10572-2022-INIT/en/pdf (accessed June 2023).

(b) having appointed solely as a result of the exercise of one's voting rights a majority of the members of the administrative, management or supervisory bodies of a legal person or entity who have held office during the present and previous financial year;
(c) controlling alone, pursuant to an agreement with other shareholders in or members of a legal person or entity, a majority of shareholders' or members' voting rights in that legal person or entity;
(d) having the right to exercise a dominant influence over a legal person or entity, pursuant to an agreement entered into with that legal person or entity or to a provision in its Memorandum or Articles of Association, where the law governing that legal person or entity permits it being subject to such agreement or provision;
(e) having the power to exercise the right to exercise a dominant influence referred to in point (d), without being the holder of that right;
(f) having the right to use all or part of the assets of a legal person or entity;
(g) managing the business of a legal person or entity on a unified basis while publishing consolidated accounts;
(h) sharing jointly and severally the financial liabilities of a legal person or entity or guaranteeing them.[7]

Screening should ideally be conducted at the outset of the proceedings, prior to any payment of advances on costs and, if possible, registration fees. However, there may be instances where a party becomes designated after the advances have already been paid, triggering the sanctions-related obligations of the actors involved during the course of the proceedings. In such situations, the institution should promptly notify its bank and will need to seek a derogation from the national competent authority in accordance with the relevant provision for any payments to be made during the proceedings or following the termination of the arbitration.

Ownership enquiries and information obtained from the parties and the results of the institution's own due diligence should be properly documented as proof of compliance with the sanctions regulation.[8] Arbitration rests on the foundation of trust between the parties involved, as well as their trust in the administering institution and the tribunal. Consequently, it is wise for institutions to provide clear explanations of the enquiry process and offer procedural guidance on subsequent steps as part of their

7. EU Best Practices for the effective implementation of restrictive measures, 22 July 2022, https://data.consilium.europa.eu/doc/document/ST-10572-2022-INIT/en/pdf (accessed June 2023).
8. The implications of the screening procedure in relation to GDPR are touched upon in the following publication. 'Caught between data protection and economic sanctions?' By Yuliya Miadzvetskaya, 7 May 2019, https://www.law.kuleuven.be/citip/blog/caught-between-data-protection-and-trade-sanctions/ (accessed June 2023).

service. Any inquiries into corporate and ownership structures should be transparent regarding their legal basis, purpose, and scope for screening.

It is important to note that institutional due diligence does not relieve the tribunal of its own responsibility to conduct sanctions checks. During the course of the proceedings, facts may emerge that reveal a party's exposure to sanctions, which the institution may not have discovered prior to referring the case to the tribunal. In practice, however, institutional due diligence considerably facilitates compliance with the sanctions for the tribunal and for the parties. In ad hoc arbitration, the tribunal will be responsible for conducting the due diligence process and for monitoring the changes in the sanction regulations throughout the proceedings.

[B] Article 4.1.(b): Derogation Related to Payment for Legal Services

Already, when the sanctions were introduced, a derogation related to legal services was established in Article 4.1.(b) of Regulation 269/2014. The article reads as follows:

> By way of derogation from Article 2, the competent authorities of the Member States may authorise the release of certain frozen funds or economic resources, or the making available of certain funds or economic resources, under such conditions as they deem appropriate, after having determined that the funds or economic resources concerned are: […]
>
> b) intended exclusively for payment of reasonable professional fees or reimbursement of incurred expenses associated with the provision of legal services.

The purpose of this provision is to facilitate access to legal services, in accordance with Article 47 of the Charter of Fundamental Rights of the European Union (the Charter), as clarified by CJEU in case *Užsieniom reikalų ministerija, Finansinių nusikaltimų tyrimo tarnyba v. Peftiev*. In the case, CJEU considered an identical provision in EU Regulation 765/2006 regarding sanctions against Belarus, finding that in exercising its discretion to decide on applications for the release of frozen funds, the national competent authorities must consider Article 47 of the Charter:

> The second sentence of the second paragraph of Article 47 of the Charter, concerning the right to an effective judicial remedy, provides that everyone has the possibility of being advised, defended and represented. […] Thus, Article 3(1)(b) of Regulation No 765/2006 must be interpreted in accordance with Article 47 of the Charter, to the effect that a freeze of funds cannot have the effect of depriving the persons whose funds have been frozen from effective access to justice.[9]

Thus, CJEU confirmed that 'legal services' are an integral part of the right to an effective remedy under the Charter.

9. Case C-314/13, ECLI:EU:C:2014:1645, §§ 25, 26 https://curia.europa.eu/juris/document/document.jsf;jsessionid = A233BE4F631E12585804B536083DADF5?text = &docid = 153579&pageIndex = 0&doclang = en&mode = lst&dir = &occ = first&part = 1&cid = 1700136 (accessed June 2023).

In the context of arbitration, the derogation in Article 4.1.(b) may come into play, e.g., in an ongoing arbitration where the advance on costs is to be paid by a listed party. Article 4.1.(b) does not explicitly specify whether it is the listed party or the recipient of the payment who should apply for the authorization. Based on the provision, however, an arbitral institution or arbitrator involved in the case as recipients of fees should, in principle, be eligible to seek authorization from the competent authority to release frozen funds. Considering the broad discretionary powers granted to the national authorities to decide on these matters, some procedural variations in each Member State are to be expected.

When submitting an application for authorization based on a derogation, the applicant needs to include certain details of the case, e.g., the name of the listed party, the purpose of the future payment, and information on bank accounts used, including the remitting, correspondent, and receiving banks involved. Additionally, evidence demonstrating the reasonableness of the preliminary fees and costs should be provided. This could involve referencing the applicable table of costs and providing the decision on the advance on costs to be paid. The specific evidence required may vary depending on the cost system employed by the administering institution, whether it be based on ad valorem or hourly fees.

Although the provision leaves the authorities discretion to decide on the conditions for the payments, the national competent authority is likely to take a cautious approach. It is the experience of the authors that one should not expect that a decision of the national competent authority will cover several consecutive payments but rather that authorization is needed for each individual transaction. All authorizations by the national competent authorities are to be reported to the European Commission. One may also expect that upon granting a derogation, the national authority will impose a deadline for the execution of the transaction and require the applicant to provide a report within a specified period of time.

In international arbitrations, legal services are provided across multiple jurisdictions, members of the tribunal may not be based in the same country as the arbitral institution overseeing the case, and one single transaction may cross multiple jurisdictions. As there are no provisions to the effect that the decision of the competent authority in one Member State should be valid or adhered to in another Member State, this implies that decisions on authorizations are valid only within the territory of the Member State where they were issued. For this reason, applications may need to be submitted in multiple jurisdictions, notwithstanding that the applications concern the same transaction. One would expect, however, that the decision of one competent authority adds value to the application process undertaken by another competent authority.

It is important to note that authorization covers the receipt of funds from a listed entity or person and does not automatically grant permission to return any unused funds. Arbitrators and institutions are advised to take this into consideration when requesting the advance on costs. Many institutions request advances to be paid in instalments throughout the proceedings. This approach may allow for a more accurate calculation of the advance on costs vis-à-vis the final costs of the arbitration. It also

means, however, that each payment is likely to require a separate application for authorization.

Any unused funds from a listed entity or person should be treated as frozen and reported to the national competent authority in accordance with Article 8, *see* below.

An additional consideration is that the application process is subject to the principle of publicity in most EU countries, including Sweden (*Sw.* offentlighetsprincipen), and thus entails the disclosure of details of the arbitration to third parties. Consequently, it is to be expected that some EU-based institutions will update their rules to include provisions on compliance, specifically addressing the disclosure obligations imposed by the sanction legislation.

[C] Article 5.1: Claims Arising out of Arbitral and Judicial Decisions

Article 5.1 provides for a derogation from the freeze of assets for the purpose of enforcing judicial decisions and arbitral awards:

> 1. By way of derogation from Article 2, the competent authorities of the Member States may authorise the release of certain frozen funds or economic resources, if the following conditions are met:
>   (a) the funds or economic resources are subject to an arbitral decision rendered prior to the date on which the natural or legal person, entity or body referred to in Article 2 was included in Annex I, 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;
>   (b) the funds or economic resources will be used exclusively to satisfy claims secured by such a decision or recognised as valid in such a decision, within the limits set by applicable laws and regulations governing the rights of persons having such claims;
>   (c) the decision is not for the benefit of a natural or legal person, entity or body listed in Annex I; and
>   (d) recognition of the decision is not contrary to public policy in the Member State concerned.
> 2. The Member State concerned shall inform the other Member States and the Commission of any authorisation granted under paragraph 1.

Article 5.1 allows for the release of frozen funds within the EU for the purpose of enforcing arbitral awards, judicial, and administrative decisions against a sanctioned party. Importantly, the article makes a distinction between arbitral awards on the one hand and judicial and administrative decisions on the other. The derogation in Article 5.1 only applies to arbitral awards rendered *before* the sanctioned party was listed, while it applies to judicial and administrative decisions rendered within the EU both before and after the listing of the party.

This requirement raises concerns regarding its coherence with the principles of effective remedy and objectives of the regulations. The aim of the economic sanctions is to hinder Russia's capacity to sustain the war against Ukraine.[10] Article 5.1 implies

10. https://www.consilium.europa.eu/en/policies/sanctions/restrictive-measures-against-russia-over-ukraine/sanctions-against-russia-explained/ (accessed June 2023).

that the enforcement of awards rendered post-designation is indefinitely halted, whereas enforcement of court judgments is permitted. The reason for the distinction between arbitral awards and decisions made by public courts is not clear.

In the views of the authors, there should be no distinction made between a court decision or judgment and an arbitral award. Both are enforceable titles as a consequence of legal proceedings in accordance with relevant laws and regulations. Courts, arbitral institutions and arbitral tribunals are providers of justice, and their decisions carry equal weight. The limitation included in Article 5.1, restricting the derogation to awards made prior to the listing, denies EU parties an enforceable remedy against sanctioned parties to the benefit of the latter. This is perhaps the most significant consequence of the article, as it contradicts the objectives of the sanction regulation, and it should be remedied by the regulator.

Furthermore, the limitation is incoherent with Article 7, which provides for the enforcement of arbitral awards in favour of sanctioned parties regardless of the time of rendering, as long as the funds credited remain frozen.

[D] Article 7: Payments due to Listed Parties under Arbitral Decisions

This article specifically addresses payments owed to the listed parties. It allows banks to accept funds transferred by third parties into the account of a listed individual or entity on the condition that any amounts deposited into those accounts are also frozen. The article is formulated as follows:

> 1. Article 2(2) shall not prevent the crediting of the frozen accounts by financial or credit institutions that receive funds transferred by third parties onto the account of a listed natural or legal person, entity or body, provided that any additions to such accounts will also be frozen. The financial or credit institution shall inform the relevant competent authority about any such transaction without delay.
> 2. Article 2(2) shall not apply to the addition to frozen accounts of:
>   (a) interest or other earnings on those accounts;
>   (b) payments due under contracts, agreements or obligations that were concluded or arose before the date on which the natural or legal person, entity or body referred to in Article 2 has been included in Annex I; or
>   (c) payments due under judicial, administrative or arbitral decisions rendered in a Member State or enforceable in the Member State concerned;
>
>   provided that any such interest, other earnings and payments are frozen in accordance with Article 2(1).

Article 7.2(c) states that the award should either be rendered or be enforceable in the Member States and, unlike Article 5.1, it treats judgments and arbitral awards equally; i.e., it does not require arbitral awards to be rendered prior to the designation of an entity or individual.

Article 7 was subject to judicial consideration by the High Court of Justice in England in the recent case of *PJSC National Bank Trust v. Mints*.[11] The case examined the impact of sanctions on civil litigation and answered the question of whether substantive judgments and arbitral awards can be rendered in favour of a designated entity after its designation, and if so, under what circumstances. The court also emphasized that the EU regulation in question applies equally to judgments and arbitral awards.[12]

The case was initiated in 2019. During the course of the proceedings, the UK Government imposed asset freeze restrictions on one of the claimants and two individuals who owned or controlled the other claimant. After the designation of the claimants, the respondents raised an objection, contending that any judgment entered in favour of the claimants would be unlawful due to the applicable sanction regime.[13]

In its judgment, the court examined both the UK and the EU sanctions, analysing the effects of Articles 7 of Regulation 269/2014 on judicial proceedings. The court observed that this provision encompasses both judgments and arbitral awards and concluded that the EU sanction regulations were not designed to differentiate between judgments and arbitral awards.[14]

The court rejected the argument that entering a judgment would violate the freeze of funds provision outlined in Article 2(1) of Regulation 269/2014:

> In order to get to this argument one has to recharacterise the entry of the judgment as a dealing in the underlying cause of action, which is not a characterisation which is apt to the EU Regulation. Nor indeed does it reflect the actual wording of Article 2 which does not mention dealing (in either part). Article 2(1) stipulates 'all funds and resources … shall be frozen'. Even if a judgment creates a fund, entering a judgment has nothing to do with frozen assets. Article 2(2) says that 'no funds or economic resources shall be made available'.[15]

Therefore, the court concluded that 'the EU Regulation does not preclude – and logically contemplates – the entry of judgments against (and by necessary implication for) a designated person after the imposition against them of sanctions'.[16]

While a judgment from the High Court of Justice in England does not serve as an authoritative interpretation of EU law, it carries weight as it relies on an analysis of the EU regulations that were incorporated into UK law until 2018. The judgment also involves thorough research into fundamental legal principles, including legality and access to courts, based on UK, EU, and international law. The analysis made by the court demonstrates that these principles are not restricted by the sanctions legislation.[17]

11. [2023] EWHC 118 (Comm) in §2 https://www.oeclaw.co.uk/images/uploads/judgments/PJSC_v_Mints_final_for_approval_and_hand_down.pdf (accessed June 2023).
12. *Ibid.*, §28.
13. *Ibid.*, §6.
14. *Ibid.*, in §§28 and 148.
15. *Ibid.*, in §33.
16. *Ibid.*, in §36.
17. *Ibid.*, in §66.

It is important to emphasize that in the *PJSC National Bank Trust v. Mints* case, the High Court of Justice addressed claims that were unrelated to sanctions and which arose prior to the designations. Based on this judgment, and in the absence of provisions to the contrary, one could also infer that arbitral awards which concern claims which arose prior to the designation of the party and that are unrelated to sanctions may be rendered in favour of the sanctioned party. However, the situation is different when it comes to claims that fall under the 'no claims' provisions in Article 11 of Regulation Nos 269/2014 and 833/2014, which will be discussed below.

[E] Article 11: 'No Claims' Provisions

Article 11 shields EU parties from having to satisfy claims caused by the restrictive measures.[18] The article reads 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, particularly 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) designated natural or legal persons, entities or bodies listed in Annex I;
>   (b) any natural or legal person, entity or body acting through or on behalf of one of the persons, entities or bodies referred to in point (a).
> 2. In any proceedings for the enforcement of a claim, the onus of proving that satisfying the claim is not prohibited by paragraph 1 shall be on the natural or legal person, entity or body seeking the enforcement of that claim.
> 3. This Article is without prejudice to the right of natural or legal persons, entities or bodies referred to in paragraph 1 to judicial review of the legality of the non-performance of contractual obligations in accordance with this Regulation.

The article bears a resemblance to its counterpart in Regulation 833/2014, with nearly identical wording. According to the wording of Article 11, it applies when a claim arises from a breach caused by the measures introduced by Regulation 269/2014 and when the claim is brought by a sanctioned entity or person or a party controlled by a sanctioned entity or person. Both criteria must be met for the provision to apply. In Regulation 833/2014, Article 11 applies to any claim brought by a Russian state-owned or controlled entity or to any Russian person, entity or body.[19]

Similar to Article 7, Article 11 follows the same logic in that it does not outright prohibit the adjudication of claims. This is supported by Article 11(2), which places the burden of proof on the sanctioned person or entity to demonstrate that satisfying the claim is not prohibited by Article 11.

18. Commission's consolidated FAQs on the implementation of Council Regulation Nos 833/2014 and 269/2014, Question 8, p. 18.
19. *See* Art. 11.1 a) and b).

Article 11 gives reason to question whether it permanently relieves non-sanctioned parties from satisfying claims arising out of the non-performance caused by sanctions. To answer this question, it is necessary to examine the history of 'no claims' provisions, which can be traced back to the UN sanctions programme against Iraq and the corresponding Council Regulation (EEC) No. 3541/92 of 7 December 1992 adopted in 1992.[20] The regulation prohibited the satisfaction of Iraqi claims related to contracts and transactions affected by United Nations Security Council Resolution 661 (1990) and subsequent resolutions.

The regulation established a 'no claims' regime that was materially similar to the one concerning claims by Iraq arising from the UN trade embargo. During the drafting process of the regulation, an explanatory memorandum was prepared. A portion of this memorandum is referenced in the case of *H Shanning International Ltd v. Lloyds TSB Bank plc; Lloyds TSB Bank plc v. Rasheed Bank* (28 June 2001):[21]

> The measures proposed herewith in order to implement paragraph 29 of UNSC Resolution 687 (1991) are based on the following specific considerations:
>
> (1) Non-enforceability of claims or prohibition to pay
>
> Paragraph 29 can be interpreted either as making claims by Iraq non-enforceable, or as establishing a prohibition to honour such claims. The practical consequences of each interpretation are different. A system of NON-ENFORCEABILITY would protect banks and exporters against claims mentioned in paragraph 29 of UNSC Resolution 687, by making it impossible for any Iraqi party to obtain a judgment in its favour unless it could prove that the contract or transaction was not affected by the embargo.
>
> However, such a system would allow claims being settled by agreement between the parties concerned. This would considerably weaken the protection granted, as it would expose non-Iraqi operators, in particular contractors, to pressure which might be exerted by the Iraqi side. It would also create uncertainty as to whether the contracts concerned would still have to be treated as valid obligations. Finally, this system would not permit the achievement of the other objective of paragraph 29, i.e., the prevention of retroactive compensation in favour of Iraq.
>
> Therefore, the Commission proposes a system of PROHIBITION TO HONOUR CLAIMS, which would allow to meet both the objective of preventing such retroactive compensation as well as the objective of an effective protection of non-Iraqi parties, and would establish clarity as regards the treatment of the contractual obligations concerned.

The case involved a claim based on a series of cross-bank guarantees relating to the delivery of operating theatres and medical equipment to Iraq. The UN sanctions against Iraq were imposed during the performance of the contract, which raised the question of whether the payment could be released under the bank guarantee. In the

20. Council Regulation (EEC) No. 3541/92 of 7 December 1992 https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A31992R3541 (accessed June 2023).
21. *United Nations Juridical Yearbook* Extract from: Chapter VIII: Decisions of National Tribunals 2001 Part Three. Judicial decisions on questions relating the United Nations and related intergovernmental organizations, Decision of House of Lords in *H Shanning International Ltd v. Lloyds TSB Bank plc*; *Lloyds TSB Bank plc v. Rasheed Bank* (28 June 2001), p. 491.

court proceedings, Lloyds, the bank issuing a counter-guarantee, sought declarations that it was 'permanently prohibited from satisfying any and all claims' by Rasheed Bank for payment under the Lloyds counter-guarantee. Eventually, the court determined that Regulation (EEC) No. 3541/92 indeed permanently prohibited the satisfaction of any and all claims made or to be made by the Iraqi parties, even if the sanctions were to be lifted.

Based on the aforementioned case law, it could be inferred that Article 11 is intended to provide permanent protection to EU parties from claims arising out of their non-performance due to the sanctions.

Apart from its implications on the merits of the dispute, the 'no claims' provision sparked discussions regarding the arbitrability of such cases.[22] In recent decades, however, jurisprudence has adopted a liberal approach towards tribunals' authority to arbitrate disputes that involve elements of public law, including sanctions. Such disputes are considered arbitrable by the legal doctrine,[23] and there is also extensive case law in support of this conclusion.[24] For instance, in the *Air France v. Libyan Arab Airline* case, the Quebec Court of Appeal rejected Air France's argument that the UN embargo against Libya rendered the dispute non-arbitrable.[25] The court asserted that 'contrary to Air France's contention, the UN Resolutions do not prohibit Air France from appointing an arbitrator. It would be illogical to assume that the regulation pertaining to the embargo prevents the parties from initiating the arbitration process, if only for the purpose of allowing the arbitral tribunal to rule on the applicability of the measures in question'.[26]

This being said, one may not rule out that courts in less arbitration-friendly jurisdictions might adopt a different approach.

[F] Article 8.1: Reporting Obligation

Article 8.1 reads as follows.

> 1. Notwithstanding the applicable rules concerning reporting, confidentiality and professional secrecy, natural and legal persons, entities and bodies shall:
>   (a) supply immediately any information which would facilitate compliance with this Regulation, such as information on accounts and amounts

22. *See*, *e.g.*, 'Sanctions and arbitrability' by Roberto Oliva, https://www.arbitratoinitalia.it/en/2022/11/11/sanctions-arbitrability/ (accessed June 2023).
23. 'Part II, Chapter 4: Authority of Domestic Courts and Arbitral Tribunals to Give Effect to Trade Sanctions', in Mercedeh Azeredo Da Silveira, Trade Sanctions and International Sales: An Inquiry into International Arbitration and Commercial Litigation (© Kluwer Law International; Kluwer Law International 2014) pp. 65-126.
24. *See*, *e.g.*, 'Arbitrability of Disputes' by Y. Fortier, 'Global Reflections on International Law, Commerce and Dispute Resolution', Liber Amicorum in Honor of Robert Briner. *See also* the article by Salomé Garnier Navacelle, Stephane de Navacelle and Julie Zorrilla 'When Arbitration and Compliance Meet Up: Analysis of Their First Interplay' https://docs.google.com/document/d/1Wo-uIY-m0QH1_YRZ1jkV9nLLDAqUtvF_/edit# (accessed June 2023).
25. Court of Appeal Canada, Province of Quebec, Registry of Montreal, No.: 500-09-009391-004 (500-05-043881-984), dated 31 March 2003.
26. *Ibid.*, section 47.

> frozen in accordance with Article 2 or information held about funds and economic resources within Union territory belonging to, owned, held or controlled by natural or legal persons, entities or bodies listed in Annex I and which have not been treated as frozen by the natural and legal persons, entities and bodies obliged to do so, to the competent authority of the Member State where they are resident or located, and shall transmit such information, directly or through the Member State, to the Commission; and
>
> (b) cooperate with the competent authority in any verification of such information.
>
> [...]

In July 2022, as a part of the seventh sanction package, the EU strengthened the reporting obligations of its subjects by imposing the duty to report, notwithstanding any obligations of confidentiality or professional secrecy which may also apply.[27] Although the EU Commission clarified that the provision 'should not cover information received as part of legal representation in court proceedings',[28] the sanction regulations do not provide any formal exemptions from the reporting obligation for legal professionals.

At the moment of writing, the Council of Europe considers a Proposal for a Directive on the definition of criminal offences and penalties for the violation of EU's restrictive measures ('the Proposal'). The Proposal clarifies that the obligation to report information shall not apply to the information that legal professionals receive from, or obtain on, one of their clients, in the course of ascertaining the legal position of their client or performing the task of defending or representing that client in, or concerning, judicial proceedings, including providing advice on instituting or avoiding such proceedings.[29]

If the aforementioned text is adopted by the Council, it will function as an exemption to the reporting obligation concerning judicial proceedings. However, the mentioned provision does not explicitly address legal services rendered in arbitral proceedings, raising concerns about its potential implications for arbitrators and party representatives involved in such cases. The obligation to report a client or a party under the threat of prosecution presents a challenge when it comes to upholding the principles of justice as well as safeguarding the independence of lawyers.

If the proposed text does not grant an exemption to legal professionals from the reporting obligation in arbitral proceedings, and if the suggested penalty for non-compliance is implemented, there is a substantial risk that it will negatively impact the willingness of EU counsel and arbitrators to accept appointments in cases involving

27. Council Regulation (EU) 2022/1273 of 21 July 2022, §5 in the recitals. https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32022R1273 (accessed June 2023).
28. Commission's consolidated FAQs on the implementation of Council Regulation No. 833/2014 and Council Regulation No. 269/2014, p. 31, Question 30.
29. Proposal for a Directive of the European Parliament and of the Council on the definition of criminal offences and penalties for the violation of Union restrictive measures, Doc. 9312/23, https://data.consilium.europa.eu/doc/document/ST-9312-2023-INIT/en/pdf (accessed June 2023).

sanctioned parties, depriving all parties of the sole effective legal remedy in the domain of international trade.

§2.04 THE LEGAL AND PRACTICAL EFFECTS OF REGULATION 833/2014 ON ARBITRATION

While Regulation 269/2014 outlines a list of individuals and entities subject to financial sanctions, Regulation 833/2014 deals with sectoral sanctions that impose limitations on the export of goods and technologies in the defence and oil sectors. The provisions of Regulation 833/2014 that are particularly relevant for arbitration include:

- Article 5b 1. (ban on acceptance of deposits exceeding EUR 100,000);
- Article 5c 1(b) (derogation related to 5b 1);
- Article 5aa (exemption for services related to access to justice);
- Article 5n (exemption on the provision of legal advisory services in arbitration); and
- Article 11 ('no claims' provision).

[A] Articles 5b 1 and 5c 1(b): Deposits Exceeding EUR 100,000

This prohibition was introduced in February 2022 as part of the second sanction package against Russia. Initially, it concerned the transactions of funds in excess of EUR 100,000 made by Russian nationals and entities from Russia. In July 2022, the prohibition was extended to include transactions made by entities *controlled* by Russian nationals or natural persons residing in Russia. The article currently reads as follows:

> [...] It shall be prohibited to accept any deposits from Russian nationals or natural persons residing in Russia, legal persons, entities or bodies established in Russia or a legal person, entity or body established outside the Union and whose proprietary rights are directly or indirectly owned for more than 50 % by Russian nationals or natural persons residing in Russia, if the total value of deposits of that natural or legal person, entity or body per credit institution exceeds EUR 100 000.

The acceptance of amounts exceeding EUR 100,000 is subject to a derogation mechanism similar to the one applied to the provision of legal services to designated individuals and entities. Under Article 5c 1(b):

> By way of derogation from Articles 5b(1) and (2), the competent authorities may authorise the acceptance of such a deposit or the provision of wallet, account or custody service, under such conditions as they deem appropriate, after having determined that the acceptance of such a deposit or the provision of wallet, account or custody service is:
>
> [...]

(b) intended exclusively for the payment of reasonable professional fees or the reimbursement of incurred expenses associated with the provision of legal services.

While the process for seeking authorization for accepting funds may mirror the one outlined in §2.03[B] above, it is important to note that authorization is necessary for any transfer of amounts in excess of EUR 100,000 originating from Russian parties or parties under Russian control, irrespective of whether they are subject to sanctions or not.

[B] Article 5aa: Exemption for Services to Ensure Access to Justice

In March 2022, by issuing Council Regulation (EU) No. 428/2022, the European Union introduced a fourth package of sanctions against Russia, which included, *inter alia*, a general prohibition to directly or indirectly engage in any transaction with publicly controlled Russian entities.[30] Since the prohibition did not include any exemptions for arbitration-related services, it created a great deal of uncertainty for arbitrators, counsel and arbitral institutions involved in arbitrations with Russian state-owned or controlled companies.

Following the joint efforts of several EU-based arbitral institutions, including the SCC Arbitration Institute, VIAC, FAI, DIS, CAM and Swiss Arbitration Centre,[31] in addressing the implications of the fourth sanctions package on international arbitration and the rule of law, Article 5aa of Regulation 833/2014 was amended through the seventh sanctions package in July 2022 to include an exemption in Article 5aa 3(g), as follows:

1. It shall be prohibited to directly or indirectly engage in any transaction with:
   (a) a legal person, entity or body established in Russia, which is publicly controlled or with over 50 % public ownership or in which Russia, its Government or Central Bank has the right to participate in profits or with which Russia, its Government or Central Bank has other substantial economic relationship, as listed in Annex XIX;
   (b) a legal person, entity or body established outside the Union whose proprietary rights are directly or indirectly owned for more than 50 % by an entity listed in Annex XIX; or
   (c) a legal person, entity or body acting on behalf or at the direction of an entity referred to in point (a) or (b) of this paragraph.
   [...]
3. The prohibition in paragraph 1 shall not apply to:

   [...]

30. §5aa of Council Regulation (EU) 428/2022 of 15 March 2022 amending Regulation (EU) No. 833/2014 concerning restrictive measures in view of Russia's actions destabilizing the situation in Ukraine https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32022R0428 (accessed June 2023).
31. *See* Joint statement of SCC, VIAC, FAI, DIS, CAM and Swiss Arbitration Centre regarding the EU's 7th sanctions package https://sccarbitrationinstitute.se/en/news/joint-statement-eu-provides-exemption-arbitration-proceedings (accessed June 2023).

> (g) 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 and if such transactions are consistent with the objectives of this Regulation and Regulation (EU) No 269/2014.

The provision establishes a few important rules to comply with when administering cases with Russian state-owned entities. First, it provides for an exemption for arbitration, meaning that the services performed by arbitral institutions and arbitrators are neither prohibited nor require authorization. It does, however, not cover the receipt of *payments* from the Russian state-owned entities, which are subject to the asset freeze regime under Regulation 269/2014. As explained in §2.03[B] above, authorization is still required for such entities.

Second, it imposes the requirement that the transaction is 'strictly necessary' to ensure access to arbitral proceedings. As known, international arbitration involves multiple services of a legal and administrative character, most of which are indispensable for the organization of the proceedings and, hence, ensuring access to justice: in addition to the adjudication itself, arbitration involves administration services by arbitral institutions, financial services by banks, translation and court-reporting services by language providers, facility lease services by hearing centres, etc.

The requirement that the transaction is 'strictly necessary' mirrors the terminology used in relation to legal services further discussed in §2.04[C] below. The regulator, however, does not provide clear guidance on its scope. The lack of clarity regarding which services are considered permitted and which are considered prohibited in the eyes of the EU regulator may discourage service providers from accepting assignments involving sanctioned parties and consequently compromise access to justice for all parties involved, sanctioned and non-sanctioned.

Furthermore, it is unclear why Article 5aa 3(g) is limited to the awards *rendered* in a Member State and does not include awards *enforceable* in a Member State. The current wording implies that any transactions related to enforcement proceedings of an award rendered, for example, in Switzerland or in England, would not qualify for the exemption. In the eyes of the authors, there is no reason to exclude arbitral awards rendered outside the EU from enforcement in the EU, and, as in the case of Article 5.1 of Regulation 269/2014, we call upon the EU regulator to clarify its intention and/or amend the provision as appropriate.

Finally, the article harmonizes the exemption with the objectives outlined in Regulation (EU) No. 269/2014, aiming to ensure adherence to the asset freeze provisions established by the same regulation.

[C] Article 5n: Exemption for Legal Services in Contentious Matters

This article was included in the eighth sanction package in October 2022, introducing, *inter alia,* a general prohibition on rendering legal services to legal persons, entities or bodies established in Russia. It also includes a couple of exemptions for legal services

necessary to ensure access to justice and the right to an effective legal remedy.[32] The article reads as follows.

> 1. [...]
> 2. It shall be prohibited to provide, directly or indirectly, architectural and engineering services, legal advisory services and IT consultancy services to:
>   (a) the Government of Russia; or
>   (b) legal persons, entities or bodies established in Russia.
>   [...]
> 5. Paragraphs 1 and 2 shall not apply to the 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.
> 6. Paragraphs 1 and 2 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 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 (16).

The exemption imposes a requirement for the legal services to be 'strictly necessary'. The scope of this criterion is commented on in the Commission's Consolidated FAQs as follows: 'As explained in Recital 19 of Council Regulation (EU) 2022/1904, the prohibition of legal services does not apply to representation, advice, preparation of documents or verification of documents in the context of legal representation services.'[33] The Commission continues: 'These exceptions are to be interpreted restrictively. The term "strictly" means that there is no other way to terminate contracts or to exercise the right of defense other than to rely on the provision of these otherwise prohibited services.'[34]

Legal representation services in arbitral proceedings are typically voluntary, granting parties the freedom to advocate for themselves. Consequently, there are concerns within the arbitration community that legal services in arbitration may not meet the criteria of being 'strictly necessary' and thus lie outside the purview of exemption. Nevertheless, the principle of equality of arms in an adversarial process implies that the parties have the same procedural rights. A scenario where one of the parties is denied access to legal advice in a foreign jurisdiction, while its counterparty retains full right to engage legal counsel and other services related to the arbitral proceedings, does not conform with this fundamental principle. Hence, the comments of the Commission raise concerns in relation to the principles of due process and the

32. Council Regulation (EU) 2022/1904 of 6 October 2022 amending Regulation (EU) No. 833/2014 concerning restrictive measures in view of Russia's actions destabilizing the situation in Ukraine.
33. Question 26 in Consolidated FAQs on the implementation of Council Regulation No. 833/2014 and Council Regulation No. 269/2014 https://finance.ec.europa.eu/system/files/2023-05/faqs-sanctions-russia-consolidated_en.pdf (accessed June 2023).
34. Provision of services related provision: Art. 5n of Council Regulation 833/2014 Frequently Asked Questions as of 21 December 2022, Question 3 https://finance.ec.europa.eu/system/files/2022-12/faqs-sanctions-russia-services-provision_en_0.pdf (accessed June 2023).

fundamental rights enshrined in the Charter. Therefore, it should provide further clarifications on the scope of this provision.

Similar to Article 5aa 3(g), this exemption is also limited to services related to enforcement proceedings of arbitration awards rendered within the EU. Considering that enforcement proceedings take place within the jurisdiction of national courts, engaging the services of a local legal counsel becomes a vital component. The wording regrettably seems to prohibit the rendering of legal services in relation to arbitral awards rendered in non-EU arbitration jurisdictions, such as Switzerland and the UK. As mentioned above, the derogations related to the enforcement of arbitral awards under Regulation 269/2014 do not include any such limitations.

The ban on legal services under Article 5n has emerged as, arguably, the most contentious component of the sanction legislation. Presently, there are two actions against the Council of Europe pending,[35] seeking to annul the ban. The applicants claim that it constitutes an infringement of the fundamental rights to protection of privacy and access to justice, interference with the right of every litigant to seek legal advice from his or her lawyer, with the principle of professional secrecy and the principle of the independence of the lawyer.

[D] Article 11: 'No Claims' Provisions

Article 11 applies to any claim brought by a Russian state-owned or controlled entity or to any Russian person, entity or body, but otherwise resembles the no-claims provisions in Article 11 of Regulation 269/2014. The implications of Article 11 are accounted for above in §2.03[E].

§2.05 CONCLUSIONS

The EU sanctions regime targeting Russia raises concerns regarding the compromise of the parties' access to justice and right to an effective remedy. While the sanctions are designed to achieve specific policy objectives, they may inadvertently hinder access to justice. The EU should assess the potential unintended consequences of proposed measures and ensure that the restrictions imposed are clear and proportionate. Engaging in a thorough impact assessment and consulting relevant stakeholders can help strike a balance between achieving the policy objectives and safeguarding the fundamental rights of the parties in judicial or arbitral proceedings.

To address the concerns raised in this chapter, the EU should revisit and amend those provisions which make a distinction between judicial and arbitral proceedings, and update the comprehensive official commentary for clear and transparent guidance

35. Case T-797/22, *Ordre néerlandais des avocats du barreau de Bruxelles and Others v. Council* (2023/C 63/79) https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri = CELEX:62022TN 0797 and Case T-798/22, *Ordre des avocats à la cour de Paris and Couturier v. Council* (2023/C 63/80) https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri = CELEX:62022TN0798& from = EN (accessed June 2023).

where needed. By incorporating mechanisms for consultation and clarification, the EU can mitigate potential challenges to access to justice while achieving its policy objectives, without undermining the rule of law.