Kluwer Arbitration Blog

When the East Meets the Far East: the Impact of Russian Sanctions on Commercial Arbitration in Asia

Justin D'Agostino (Herbert Smith Freehills) · Thursday, April 30th, 2015 · Herbert Smith Freehills

and Brenda Horrigan and Rebecca Soquier, Herbert Smith Freehills LLP, Shanghai

The sanctions arising out of the Ukrainian crisis have led commercial entities to consider their options for resolving current or potential disputes. In this post, we consider the impact of the sanctions against Russia on the future of dispute resolution for Russian entities and individuals considering doing business in Asia.

Background on the Russian Sanctions

The sanctions imposed on Russia in response to its intervention in Ukraine were first adopted in March 2014 by the US, the EU and Canada. The principal measures included travel restrictions and financial sanctions against persons (both individuals and entities) who were understood to bear responsibility for the Ukrainian crisis. Further states followed suit, and sanctions were subsequently amended to broaden both their material and territorial scope. Restrictions were imposed on additional individuals and entities, notably government-owned entities such as Sberbank (Russia's largest bank), Rostec (a major industrial company), Gazprom, Gazprom Neft, Lukoil, Surgutneftegas and Rosneft (Russia's biggest oil and gas companies). Russia's financial, energy and defense sectors have been affected, which in turn has impacted Russian parties' ability to trade and invest abroad.

Key Provisions

The key issues are as follows:

1) The sanctions do not allow parties to excuse themselves from the performance of their contractual obligations. Article 2(5) of EU Council Decision 2014/145/CFSP of 17 March 2014 states the following:

> [persons listed under the sanctions] shall not be excused from making a payment due under a contract entered into prior to the date on which such person was listed, provided that the Member State concerned has

> determined that the payment is not directly or indirectly received by the [persons listed].

2) The sanctions do not entitle the parties to claim compensation where contractual performance is suspended or terminated as a result of the sanctions. Article 11(1) of Council Regulation (EU) No 833/2014 of 31 July 2014 provides in its relevant part:

> No claims in connection with any contract or transaction the performance of which has been affected . . . by the measures imposed under this Regulation . . . shall be satisfied, if they are made by [Russian persons or their representatives].

3) The sanctions do not prohibit a party from seeking juridical review of whether the non-performance of contractual obligations was in accordance with the sanctions. Article 11(3) of the same EU Regulation sets out that the prohibition of bringing such claim for compensation

> "is without prejudice to the right of the [persons referred to under the Regulations] to judicial review of the legality of the non-performance of contractual obligation in accordance with the Regulation."

Therefore, it is unlikely that an arbitral tribunal would decline to review a claim on the basis that it involves issues arising out of the sanctions.

Although these rules may appear straightforward, businesses will find that the sanctions are challenging to analyze and address in terms of both their practical and legal ramifications. We address some of the concerns below.

Concerns arising out of the sanctions

It has been suggested that, in response to the sanctions, certain Russian companies will now insist on Russian law to govern any foreign-related contract, and will agree to arbitration only in Russia or in other countries that have not imposed sanctions against Russia. While it is by no means clear that this is a universal approach, we are aware of anecdotal evidence that certain Russian parties, and their foreign counterparties, are actively seeking alternative places of arbitration.

First, there are concerns that arbitrators residing in, or holding the citizenship of, states that have imposed sanctions might decline to act in disputes involving sanctioned Russian parties or involving issues relating to the sanctions. The arbitrators would need to consider whether their own country's sanctions might be seen to affect their impartiality or independence. Justifiable doubts as to the arbitrator's lack of independence or impartiality would be valid grounds to challenge the arbitrator's appointment under several arbitration institutions' rules. The arbitrator would also need to consider whether there are any risks that any award or

orders made would be in a violation of his or her own national law.

Second, there is a risk that that any ensuing award would not be enforceable either in Russia (on the grounds that such enforcement would violate fundamental principles of Russian law) or elsewhere (on the grounds that enforcement would contravene sanctions regulations).

Third, restrictions imposed on access to funds and travel may cause significant practical difficulties, eg in securing parties' attendance at hearings.

As of April 2015, the states that have imposed sanctions on Russia include the U.S., Canada, member states of the EU, Switzerland, Japan and Australia. As several commentators have noted, the list of alternative places of arbitration is relatively short, and includes mainly Asian jurisdictions.

Looking towards the Far East

Against this backdrop, Russian entities appear to be looking towards the East, where the combination of well-established arbitration institutions within arbitration-friendly (and sanctions-free) jurisdictions is perceived as an attractive alternative to arbitration in the US or Europe.

Both the Hong Kong International Arbitration Centre (HKIAC) and Singapore International Arbitration Centre (SIAC) have been quick to express their enthusiasm and ability to accommodate Russia-related disputes.

Both Hong Kong and Singapore are Model Law jurisdictions, whose legal systems are well developed. The Hong Kong and Singapore courts have significant experience in handling arbitration-related matters, both in terms of providing assistance during the course of the proceedings and with respect to post-award applications, and both are noted for their pro-arbitration views.

Neither Hong Kong nor Singapore has yet imposed sanctions on Russia, thereby reducing the risk of infringing sanctions regulations.

Both HKIAC and SIAC have multilingual secretariats, staffed with counsel of both common law and civil law backgrounds. HKIAC has taken a further step by issuing a version of its Administered Arbitration Rules in Russian. Users of both SIAC and HKIAC have access to emergency and expedited arbitration procedures, a potentially more efficient and cost- effective approach to resolving disputes.

Given the current trade restrictions with most of the Western countries, many Russian entities have increased their interest in securing further business with the Far East.[1)] We have seen, for example, Chinese and Russian companies enter into a number of trade, energy and finance agreements back in recent months. It would not be surprising if both Hong Kong and Singapore also eventually see an increase in arbitrations seated in their jurisdictions and / or administered by their respective arbitration institutions as disputes arise out of these agreements in future years.

To make sure you do not miss out on regular updates from the Kluwer Arbitration Blog, please subscribe here. To submit a proposal for a blog post, please consult our Editorial Guidelines.

References

↑1 Lucy Hornby, "China and Russia set to finalise gas deal", Financial Times, 8 March 2015.

This entry was posted on Thursday, April 30th, 2015 at 12:38 am and is filed under Arbitration, Asia-Pacific, Russia, Sanctions
You can follow any responses to this entry through the Comments (RSS) feed. You can skip to the end and leave a response. Pinging is currently not allowed.