Kluwer Arbitration Blog

The Enforcement of Awards Against Sanctioned Parties: Mission (Im)possible?

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On 24th of February 2022, the Russian Federation commenced a full-scale and open invasion of Ukraine after annexation of Crimea and eight years of hiding behind its puppet republics, the so-called Donetsk and Luhansk People's Republics. The main difference between the start of armed conflict in the Donbas region in 2014 and the start of the open invasion in 2022 is the lightning-fast reaction of the world nations and their leaders. Since the commencement of full-scale Russia's aggression, international partners of Ukraine imposed a list of sanctions against Russia's regime and their number continues to grow. The list of these hard-hitting sanctions includes individual sanctions, sectoral sanctions such as oil price cap, ban on import and export, assets freeze and many others. In fact, as of November 2022, the Russian Federation is the most sanctioned country in the world.

International sanctions against Russia have been previously discussed on the Blog from the perspective of the EU (here and here), the US (see here) and in relation to potential investment claims (in particular under MFN clauses).

Alongside the massive sanctions campaign, a number of victims are seeking to initiate court and arbitration proceedings against the Russian Federation for the caused damages. "Russia will pay" project reports that as of September 2022, the total number of direct documented damages to both residential and non-residential buildings amounts to more than USD 127 billion.

Ukrainians continue to incur damages and losses every day, so now many victims are wondering whether there are any chances that they can get compensation via blocked or frozen assets of Russian oligarchs and Russia itself.

Legal Framework of Sovereign Immunity From Jurisdiction

The major cornerstone that one may face is the alleged impossibility to submit a damage claim against a foreign state and consequently enforcing judgment or award due to its sovereign immunity.

Sovereign immunity is a principle of customary international law that envisages the rule of sovereign equality of states. In other words, no state can be subject to the jurisdiction of another

state. International law knows two types of sovereign immunity: absolute immunity (total ban on proceedings against a foreign state unless such foreign state gives its consent) and restrictive immunity (state is entitled to immunity unless certain exception applies). The doctrine of restrictive immunity deprives state of immunity if it is engaged in various commercial activities (so-called immunity exceptions). Current legislation of most states (*i.e.*, Article 3 of the 1985 Canada State Immunity Act and Section 1(1) of the 1978 UK State Immunity Act) and international legal instruments provide for restrictive immunity that enables submission of claims against foreign states concerning their commercial transactions and activities. Thus, immunity of a foreign state can be overcome if such state gave its consent to proceedings or the state's activity falls within any of immunity exceptions.

Legal Framework of Sovereign Immunity From Execution

Even though the restrictive immunity approach allows proceedings against a foreign state, the waiver of immunity from jurisdiction does not entail waiver of the state's immunity from execution.

In general, the state's immunity from execution excludes the government's measures of constraint against the property of another state to satisfy the demands and requests of the claimants, creditors under the foreign court judgments and arbitral awards. That said, international treaties, such as the UN Convention on Jurisdictional Immunities in its Article 21 stipulates an exhaustive list of assets that are protected by sovereign immunity from execution. That list includes property used for diplomatic purposes, central bank accounts, military property and other assets that are used for official state purposes.

At the same time, the foreign state's assets that are used for commercial activities and not for state purposes are not protected by sovereign immunity from execution. To establish so, the courts usually review whether a certain activity involving the assets in question could be engaged by a private person, and not only by the sovereign. Moreover, the mentioned test and, consequently, the measures of constraint can apply to the assets that are usually used for the state purposes (such as central bank accounts) if they also have been used for commercial purposes.

That said, to lift the immunity from execution, the claimant seeking enforcement of the arbitral award should demonstrate that neither the state and/or its agencies, nor their assets are entitled to immunity protection due to their engagement in commercial activities.

The Sanctions' Impact on the Enforcement of Arbitral Awards

The recognition and enforcement of arbitral awards take place under the umbrella of the United Nations Convention on Recognition and Enforcement of Foreign Arbitral Awards. In particular, it provides limited grounds for the refusal to enforce an arbitral award. One of the most commonly seen grounds to refuse the enforcement of an arbitral award is if it is contrary to the public policy of the country where the enforcement is sought.

As far as enforcement of the award against sanctioned persons or entities is concerned, there is still no absolute consensus on whether the sanctions regime constitutes a public policy of the state.

Some national courts may refuse to enforce awards against sanctioned parties since such enforcement contradicts public policy, even though there would be no sovereign immunity bars. The rationale behind such a conclusion might be an integration of sanctions regulations into the public order of the state. Moreover, the national court may consider that such enforcement would violate *international* public policy if one of the parties is sanctioned under the EU Regulations (previously discussed here and here) that constitute domestic law of the EU members.

At the same time, it would be too premature to state that national courts would automatically refuse the enforcement of the award if it involves sanctioned legal entities or persons. Such risks indeed exist; however, the courts of arbitration-friendly jurisdictions might decide that the enforcement of awards involving sanctioned entities or persons should be permitted with certain caveats. That said, the national courts would analyze particular circumstances of the case and decide whether the award can be enforced, and if yes, under which reservations such enforcement is possible. For instance, to enforce the award via frozen assets, the claimant has to seek authorization from the relevant authorities to release frozen assets to satisfy the claims.

The Terrorism Sanctions as Possible Option?

Another option that might in some part facilitate the enforcement of arbitral awards against sanctioned entities or persons for acts of terrorism is a designation of a state as a sponsor of terrorism. However, the problem is that a very limited number of states have legislation that enables this "terrorism" designation. For instance, the United States has legal authorization to designate a state as a "state sponsor of terrorism" (*Section 620A of the Foreign Assistance Act of 1961*). The Secretary of State determines the state as a sponsor of terrorism if such a state "*repeatedly provided support for acts of international terrorism, such as assassinations or financing terrorist groups*".

In that case, the matter of enforcement of awards against a terrorist party, including a state sponsor of terrorism, its agencies and instrumentalities shall be governed by the Terrorism Risk Insurance Act of 2002. Under this law, a person or entity that has an award against a terrorist party, including a state sponsor of terrorism for acts of terrorism, could enforce it in the United States and seek satisfaction of its claims via blocked or frozen assets of the state sponsor of terrorism, its agencies and instrumentalities.

It is important to stress that the Terrorism Risk Insurance Act enables the so-called "automatic" enforcement of the award against a state sponsor of terrorism only if the award concerns claims for acts of terrorism. As to the other awards, it is highly possible that their enforcement could be possible only under special reservations, such as an authorization from the relevant authority.

Enforcement of the Award: to Be or Not to Be?

Even though the enforcement of the awards against the sanctioned entities and persons, especially against Russia, is a highly discussed issue now, it is difficult to assess the real impact of sanctions on the enforcement of an arbitral award. It is clear for sure that the claimant seeking to enforce the award against the sanctioned entity or person would face difficulties with that. First of all, the claimant should overcome the sovereign immunity bar and explain that the asset is not entitled to

immunity from execution. Secondly, and more importantly, the claimant has to demonstrate that enforcement of an award against the sanctioned entity in no way the violates public policy of the state. At the present moment it is hard to predict the real possibilities of such enforcement, so the one thing that remains for us is to monitor how that issue will develop in practice.

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