Kluwer Arbitration Blog

Navigating Disputes with Sanctioned Russian Parties: Key Solutions Offered by the Higher Regional Court of Berlin

Almira Wissenberg · Wednesday, September 25th, 2024

In a decision of 1 June 2023 (Case No. 12 SchH 5/22) that was praised as landmark, the Higher Regional Court of Berlin (Kammergericht) ("KG") addressed some of the legal issues arising from the complex dispute between Siemens and Russian Railroads ("RZhD") concerning the unilateral termination of an electric trains maintenance and repair contract by Siemens due to EU sanctions. The key issues of the KG's decision are (1) the service of documents through public notification and (2) the declaration of the admissibility of arbitration. In this post, both issues are examined through the lens of recent Russian case law aiming to foster a discussion on the solutions proposed by the KG and their relevance in similar cases.

Straight to Service Through Public Notification?

In October 2022, the KG requested through the Russian Ministry of Justice the service of documents to RZhD in accordance with the 1965 Hague Service Convention ("Hague Convention"). The latter forwarded the request to the Arbitrazh Court of Moscow ("ACM"), which refused to comply with this request because it concluded that compliance with the request would violate the fundamental principles of Russian law and contradict the public policy of the Russian Federation. The higher courts upheld this decision, specifying that the KG's request for service was "illegal and aimed at delegalizing the procedural legal relations established by the ACM between Siemens and RZhD" and compliance with it would contradict the decisions of the ACM prohibiting initiation of arbitration at the VIAC dated August 24, 2022, October 26, 2022, and November 8, 2022.

As a result, the KG resorted to service by public notification, i.e., by posting a notice on an analog or digital notice board of the court, under Section 185 No. 3 of the German Civil Procedure Code ("ZPO"). This provision allows resorting to service through public notification in case service abroad is not possible or does not hold out prospects of success. In this case, service abroad had failed.

Generally, German courts assess whether service abroad holds out prospects of success under Section 185 No. 3 ZPO based on the case's specifics, with success deemed unlikely if it can be assumed that no legal assistance will be provided or that this decision will take an unreasonably long time (*Comp. German Federal Court of Justice (Bundesgerichtshof), decision of 20.01.2009 –*

VIII ZB 47/08, NJW-RR 2009, 855, Rn. 13). The Russian case law from the last two years indicates that almost all requests for service to sanctioned Russian parties under the Hague Convention coming from EU countries were refused. May, therefore, the recent practice of Russian courts allow German parties to argue that German courts shall resort to service by public notification right away, without waiting for the request for service to be denied, in cases involving a sanctioned Russian party?

Although Russian courts quite consistently refuse requests for service under the Hague Convention, their approach to reasoning for such non-compliance is rather inconsistent. On the one hand, they mostly conclude that compliance with a request would violate "the fundamental principles of Russian law and contradict the public policy of the Russian Federation." On the other hand, their path to this conclusion is each time paved with a different reasoning, not allowing to identify decisive circumstances and factors that would enable the assessment of the prospects of a request for service.

In this case involving Siemens and RZhD, Russian courts highlighted earlier anti-suit injunctions from the ACM as a decisive factor for refusing to comply with the request for service. However, in another recent case involving a request for service from Italian authorities to Gazprom Export, the 13th Arbitrazh Appeal Court concluded that the absence of such anti-suit injunctions does not prevent Russian courts from rejecting the request for service if they find that compliance therewith "may harm the sovereignty and security of the Russian Federation or violate the fundamental principles of Russian law."

The current Russian case law on requests for service under the Hague Convention exposes inconsistency even within the decisions of the same court. The Arbitrazh Court of St. Petersburg refused to comply with the requests for service to Gazprom Export from Luxembourg, German, French, and Polish authorities each time offering vague reasoning, such as the "absence of notice of the proceeding abroad to the Russian party" or "non-friendly nature of the actions of the foreign state." Nonetheless, the same court complied with a request from Croatian authorities to Gazprom Export last year despite Croatia being listed as a "non-friendly" country by the Russian Government. This decision did not elaborate on the court's motives.

The lack of clear and consistent legal reasoning for refusing requests for service under the Hague Convention, combined with rare precedents where Russian courts complied with such requests for unknown reasons, makes it challenging to assume that no legal assistance will be provided and, therefore, argue that such serving may not hold out any prospects of success. Nevertheless, the same facts could actually lend more plausibility to the position that the absence of legal certainty due to inconsistent court practice turns the prospects of success into a remote contingency and shall allow German courts to move straight to service by public notification, while keeping in mind all the traps and pitfalls of this method.

Contrasting Approaches to Enforceability of Arbitration Agreements

Another issue determined by the KG in its decision was the enforceability of the arbitration agreement as an element of the threefold test for the admissibility of arbitration under Section 1032 No. 2 ZPO. The ACM in its prohibition to initiate arbitration at the VIAC, on the contrary, determined that due to the imposed sanctions, the arbitration agreement was unenforceable, thereby

establishing the exclusive jurisdiction of the Russian courts. Courts in both countries demonstrated opposite approaches to the same circumstances.

First, the KG found the arbitration agreement to be enforceable, stating that access to arbitration must be guaranteed despite sanctions and supporting its conclusion with the clarifications of the VIAC regarding access of sanctioned parties to arbitration. In contrast, the 9th Arbitrazh Appeal Court in a parallel proceeding between the parties addressing the termination of the contract between them did not accept the official clarification of the VIAC as evidence of the enforceability of the arbitration agreement, stating that this clarification supports the opposite conclusion because it contains various reservations, *e.g.*, that this clarification is not specific to a particular case, disclaimers regarding any liability for actions taken based on this clarification, etc.

Furthermore, the KG found that the amendments to the Russian Arbitrazh (Commercial) Procedure Code ("APC") regarding the exclusive jurisdiction of Russian courts for disputes involving sanctioned parties were not relevant to the question of admissibility of arbitration since their legal effect should be assessed in the arbitration proceedings. The ACM, by contrast, based its above-mentioned decision on these amendments, namely, Article 248.1(4) APC, which grants Russian courts exclusive jurisdiction in case the arbitration agreement is unenforceable due to the application of sanctions, that prevents access to justice. The ACM followed the approach of the Russian Supreme Court developed in 2021 (see details here), where sanctioned Russian parties do not even need to prove the impact of sanctions on the arbitration agreement's enforceability, as the sanctions alone hinder access to justice for Russian parties and raise concerns regarding fair trial guarantees in the sanctioning states.

As long as Russian courts keep adhering to this approach, allowing Russian parties to walk away from an arbitration agreement, we can expect the same outcome in similar cases. Although this is unlikely to affect the position of German courts on the enforceability of arbitration agreements, German parties may consider this when assessing the practicality of defending their interests in Russian courts.

Prospects, Challenges, and Strategic Considerations

The KG's decision suggested solutions for handling important procedural issues in disputes involving sanctioned Russian parties. While not undermining the significance of this step, it is still open for discussion whether these solutions can be effectively utilized in similar cases.

In the present case, the KG found that the arbitration was indeed admissible. However, the ACM had already ruled in favour of RZhD, finding that the termination of the contract due to EU sanctions was invalid: despite this contract being governed by German law, the ACM concluded that economic sanctions were deemed contrary to Russian public policy. Therefore, RZhD seems unlikely to have an incentive to participate in arbitration in Vienna.

Nevertheless, even if it initially seems that all sanctioned Russian parties have little incentive beyond withdrawing from arbitration agreements to resolve disputes in Russian courts, various factors could influence their decision.

First, the resolution of a dispute in Russian courts does not necessarily stop the proceedings abroad, while the outcome of these proceedings may put the Russian party's assets abroad at risk.

Second, a declaratory relief granted under Section 1032(2) ZPO makes recognition of a Russian court's decision impossible in Germany. Third, even if the APC allows one-sided change of forum, it still does not allow unilateral change of the applicable law governing the merits, which is often foreign law. Finally, bringing a dispute to a state court undermines one of the primary reasons for concluding an arbitration agreement – confidentiality, which is not inherently available in state courts (see *M.L. Galperin, Living and Dead Water of the Russian Jurisdiction. On the Application of Art. 248.1 of the APC RF, Vestnik ekonomicheskogo pravosudiya RF, No. 11, 2023*).

Additionally, withdrawing from an arbitration agreement may adversely affect relations of Russian parties with partners from "friendly" and "neutral" jurisdictions. Individual precedents attempting to extend the described approach to "neutral" forums do not help build trust with partners. For example, in June 2023, the Arbitrazh Court of St. Petersburg expressed doubts that a sanctioned Russian party may be guaranteed a fair trial at the HKIAC, attributing this, *inter alia*, to the UK's influence over Hong Kong's legal system.

At last, while numerous anti-suit injunction applications from sanctioned Russian parties are currently pending in Russian courts, it remains to be seen whether the KG's solutions prove effective for Siemens and, therefore, may be recommended in similar cases.

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