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# Contracts affected by economic sanctions: Russian and international perspectives.

KOTELNIKOV, A.

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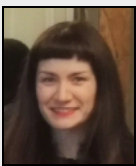
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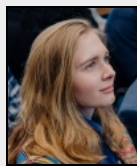
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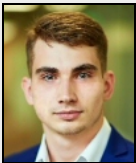
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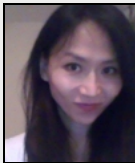
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## Contracts Affected by Economic Sanctions: Russian and International Perspectives by A. Kotelnikov

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# Contracts Affected by Economic Sanctions: Russian and International Perspectives

Andrey Kotelnikov\*

## Abstract

*Economic sanctions, particularly unilateral ones, are an increasingly popular instrument of foreign policy. Some states have extensive experience in adopting them and in resolving private disputes arising from such measures. For other countries, this practice is more recent and their sanction regimes are not as mature. Against the background of post-2014 sanction regimes targeting Russia and its counter-sanctions, this article considers the primary aspects of the impact sanctions have on the private contractual sphere. These include qualification of sanctions as a ground for invalidity of contracts and as impediment excusing debtors from the performance of their obligations. The article begins by analysing the theoretical framework developed in international doctrine and practice. It highlights the differences between the application of sanctions by domestic courts and by arbitral tribunals and considers their significance. Alongside its international counterparts, the article considers Russian domestic statutory regulation, which is well-developed and similar to that in other civil law European jurisdictions. Although it is possible to hypothesise on the possible judicial approaches, available Russian case law on this subject remains scarce and occasionally inconsistent. The avenues for further development of fundamental approaches in the practice of courts and arbitral tribunals are explored in the conclusion.*

## 1. Introduction

Over recent decades, the interest of legal experts from Russia and the Commonwealth of Independent States (CIS) in the subject of economic sanctions had been mostly theoretical. This peculiar political instrument typically concerned Russian and CIS scholars as a phenomenon of public international law.<sup>1</sup> In the realm where sanctions are traditionally of particular significance for arbitration scholars, namely the application of mandatory rules by arbitral tribunals, the majority of relevant examples were often drawn from the European and United States (US) practice.<sup>2</sup> The previous experiences of the Cold War era, such as the 1982 US Siberian Pipeline Sanctions targeting the USSR's construction of the Yamal gas pipeline to Europe,<sup>3</sup> seemed to have left a more noticeable footprint in international legal discourse than in the works of Soviet legal authors.<sup>4</sup>

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<sup>1</sup> See eg И.И. Лукашук, *Международное право: особенная часть* [II Lukashuk, *International Law: Particular Institutions*] (Wolters Kluwer, Moscow, 2005) 407. Hereinafter, translations and transliterations of Russian names, terms and phrases are my own – AK.

<sup>2</sup> See eg the leading Russian work on this subject: А.Н. Жильцов, *Применимое право в международном коммерческом арбитраже (императивные нормы): дис. ... канд. юрид. наук*, МГИМО, М., 1998. 214 с. [AN Zhiltsov, *Applicable Law in International Commercial Arbitration (Mandatory Rules)* (PhD thesis, MGIMO, Moscow 2014) 214.

<sup>3</sup> Controls on Exports of Petroleum Transmission and Refining Equipment to the USSR, 47 Fed Reg 141 (5 January 1982).

<sup>4</sup> Bernard Audit, 'Extra-territorialité et commerce international—L'affaire du gazoduc sibérien' (1983) *Revue Critique de Droit International de la Haye* 401.

This state of relative indifference began to change in 2014. Following the conflict in Ukraine and subsequent political developments, many Western countries, including the United States<sup>5</sup> and the European Union (EU),<sup>6</sup> adopted restrictive measures targeting economic relations with Russia. The Russian Federation responded by introducing its own counter-measures targeting the relations with the sanctioning states.<sup>7</sup> The co-existence of mutually imposed sanction regimes affected a large number of private players, making the performance of some contractual bargains impossible and rendering entire lines of business obsolete due to illegality. As a result, the interest in sanctions has also increased in Russian legal academia and among the legal profession.<sup>8</sup>

It is notable that the sanctions instruments typically fail to regulate their consequences for the private contractual relations which they target. Thus, it remains a matter for domestic courts and arbitral tribunals on the basis of the applicable rules of law to ascertain whether the relevant measures constitute a valid excuse for non-performance of a contract or a ground of contractual invalidity.

Undoubtedly regrettable from the political and economic perspectives, the current state of affairs is also curious in terms of its potential for the development of contract law and international private law. It creates numerous opportunities for clarifying the legal position in these and other areas. In particular, the ongoing sanctions stand-off transforms the issue of whether the court or tribunal should take a foreign prohibition into account from a theoretical possibility into a practical everyday reality.

At the political level, Russia has on many occasions expressed displeasure with the Western sanctions.<sup>9</sup> The EU and US reactions to Russian counter-measures had been mixed, but the general tenor can be described as surprise and disapproval.<sup>10</sup> Under those conditions, the problem of whether the foreign mandatory rules of such nature should be applied by arbitral tribunals and domestic courts becomes more obvious and acute.

Against this background, it is instructive to consider how the Russian law as applied by Russian courts and arbitral tribunals has dealt with the issue of the sanctions' impact on private contracts. What kinds of contractual cases made it to the Russian courts and tribunals over the

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<sup>5</sup> For the overview of the measures in question, see: The US Department of State, 'Ukraine and Russia Sanctions' <<https://www.state.gov/ukraine-and-russia-sanctions>> accessed 15 December 2019.

<sup>6</sup> For the overview of the measures in question, see: Council of the EU, 'EU sanctions against Russia over Ukraine' <<https://www.consilium.europa.eu/en/infographics/eu-sanctions-against-russia-over-ukraine>> accessed 15 December 2019.

<sup>7</sup> Federal Law of 4 June 2018 No.127-FZ 'On Measures (Countermeasures) against Unfriendly Actions of the United States of America and Other Foreign States'; the Decree of the President of Russian Federation of 6 August 2014 No 560 'On the Application of Certain Special Economic Measures to Ensure the Security of the Russian Federation' (restricting the import into Russia of certain agricultural products originating in the countries that imposed sanctions on Russia); and the Decree of the President of Russian Federation of 22 October 2018 No 592 'On Special Economic Measures in Connection with Ukraine's Unfriendly Actions towards Citizens and Legal Entities of the Russian Federation' (introducing restrictive measures against certain enumerated individuals and legal entities of Ukraine, including the blocking (freezing) of their bank accounts and other property in Russia and a ban on withdrawal of capital from Russia).

<sup>8</sup> See eg this sizeable collection of articles: Экономические санкции против России: правовые вызовы и перспективы (Сборник статей) / Под ред. С.В. Гландина, М.Г. Дораева. М., 2018 [SV Glandin, MG Doraev (eds), Moscow, *Economic Sanctions against Russia: Legal Challenges and Prospects* (Moscow 2018)].

<sup>9</sup> See eg BBC News, 'Vladimir Putin: Sanctions are Harmful for Everyone' (5 June 2018) <<https://www.bbc.co.uk/news/world-europe-44364429>> accessed 15 December 2019.

<sup>10</sup> Stefano Vergine, 'Conte to Putin: EU sanctions on Russia make Italy 'sad' (5 July 2019) <<https://euobserver.com/foreign/145376>> accessed 15 December 2019.

five years since the introduction of sanctions? Have the approaches they adopted been broadly similar to the fundamental notions developed in international practice? Is it possible to predict the outcome of similar disputes in the future? These are the questions on which this paper seeks to shed some light.

As a matter of structure, this paper will address the following issues in turn:

1. The essence and types of economic sanctions.
2. The conditions for applicability of sanctions by courts and arbitral tribunals as a matter of private international law.
3. The influence of sanctions on the contractual relations between the parties in international trade. The two most important aspects here are the invalidity of a contract, whether in full or in part, and the impossibility of performing an obligation.

## 2. Nature and Qualification of Economic Sanctions

It is customary to include a host of measures, such as embargoes, boycotts, restrictions on financing, asset freezes, travel bans and diplomatic measures, under the umbrella term ‘sanctions’.<sup>11</sup> It may be useful to begin, however, by pointing out that the term ‘sanctions’ itself, as far as the Russian legal doctrine is concerned, is not entirely uncontroversial.

Legal doctrinal sources, both in Russia and elsewhere, suggest that there are many approaches to the definition of the acts and actions which must be called ‘sanctions’ *stricto sensu* and the similar phenomena that ought to be designated by some other term. Thus, VA Vasilenko included within the definition of ‘sanctions’ all measures of legitimate coercive character, whether adopted by individual States or by international organisations, and whether involving the use of armed forces or not. This definition would include, among other things: retorsion, reprisal, self-defence, coercive measures of international organisations, and so on.<sup>12</sup> GI Kurdyukov and MV Keschner, after a detailed analysis of various theoretical approaches,<sup>13</sup> conclude that only the measures that fall within the framework of the collective security system, mainly those envisioned in the United Nations (UN) Charter provisions on collective security, should properly be called sanctions. The unilateral measures by individual States are not sanctions; such measures are lacking legitimacy because the principle of sovereign equality militates against the unilateral imposition of sanctions by one State against another.<sup>14</sup>

Scholarly writings from outside Russia rarely draw such a clear distinction. For example, one article points out that a broad spectrum of possible economic sanctions is available to the UN, as well as to the European Union and individual States.<sup>15</sup> Another researcher in a study of the economic effects of unilateral US trade restrictions against various States takes it as a starting

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<sup>11</sup> D Cortright and G A Lopez (eds), *Smart Sanctions: Targeting Economic Statecraft* (Rowman & Littlefield, 2002) 10-12.

<sup>12</sup> В.А. Василенко, *Международно-правовые санкции*. [VA Vasilenko, *Sanctions in International Law*] (Kyiv 1983) 68.

<sup>13</sup> For more details, see: Курдюков Г.И., Кешнер М.В. *Соотношение ответственности и санкций в международном праве: доктринальные подходы*. Журнал российского права 2014. N 9 [GI Kurdyukov, MV Keschner, *The Correlation Between Responsibility and Sanctions in International Law: the Doctrinal Approaches*. The Journal of Russian Law 2014. N 9] 103 - 115.

<sup>14</sup> *ibid* 111.

<sup>15</sup> E Geisinger and others, ‘The Impact of International Trade Sanctions on Contractual Obligations and on International Commercial Obligations’ [2012] 4 International Business Law Journal 405, 437.

point that the term ‘sanctions’ will be most suitable to refer to these measures.<sup>16</sup> Some authors actively discuss, for example, why, according to the empirical data, unilateral sanctions adopted by one State produce the desired effect more often than multilateral sanctions adopted within the framework of international organisations.<sup>17</sup> Both Russian<sup>18</sup> and international<sup>19</sup> media consistently use the term ‘sanctions’ when they cover the adoption of the United States, European Union and Russian unilateral restrictive measures in connection with the events in Ukraine. In everyday parlance in both Russian and English languages, the word ‘sanctions’ has the same broad meaning.

Thus, even while recognising the possible validity of the terminological distinction between ‘sanctions’ in the strict sense (adopted primarily within the UN) and other international legal measures of coercion of similar character, it must be borne in mind that this difference currently seems obvious only for a small number of lawyers and legal scholars. Therefore, consciously taking no position in this debate, it seems appropriate – for the sake of simplicity if nothing else – to continue using the expression ‘sanctions’ in this paper as a generic term.

In essence, sanctions are regulatory measures that impose restrictions on dealings with a target country, as well as companies and individuals of that country. The concrete prohibitions that a sanctions programme may adopt are numerous. These may include export and import prohibitions in relation to certain goods and services (trade sanctions), the prohibition of financing, transfer of funds, asset freezes (financial sanctions) and other measures.<sup>20</sup>

It is crucial to draw a distinction between sanctions imposed by the UN Security Council and all other kinds of measures proclaiming themselves to be ‘sanctions’. According to art 41 of the UN Charter,

“The Security Council may decide what measures not involving the use of armed force are to be employed to give effect to its decisions, and it may call upon the Members of the United Nations to apply such measures. These may include complete or partial interruption of economic relations and of rail, sea, air, postal, telegraphic, radio, and other means of communication, and the severance of diplomatic relations.”

Art 25 of the UN Charter makes it an international legal obligation for every United Nations Member State to accept and implement the decisions of the Security Council.

At the other end of the spectrum lie unilateral sanctions, i.e. those measures imposed by individual states acting individually, or under the auspices of a regional organisation such as

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<sup>16</sup> BR Early, ‘Alliances and Trade with Sanctioned States: A Study of US Economic Sanctions, 1950-2000’ (2012) 56 (3) *Journal of Conflict Resolution* 547.

<sup>17</sup> Some researchers dispute the accuracy of this premise. See eg N Bapat, T Clifton Morgan. ‘Multilateral versus unilateral sanctions reconsidered: A test using new data’ (2009) 53(4) *International Studies Quarterly* 1075.

<sup>18</sup> See eg RBC, ‘The European Council endorsed the introduction of sectoral sanctions against Russia’ (31 July 2014) <<http://www.rbc.ru/politics/31/07/2014/5704200f9a794760d3d40639>> accessed 15 December 2019.

<sup>19</sup> See eg The Guardian, ‘Ukraine crisis: Russia warns of reaction to fresh EU economic sanctions’ (6 September 2014) <<https://www.theguardian.com/world/2014/sep/06/russia-eu-economic-sanctions-ukraine>> accessed 15 December 2019.

<sup>20</sup> M Azaredo da Silveira, ‘Chapter 7: Economic Sanctions, Force Majeure and Hardship’, in F Bortolotti and D Ufot (eds), *Hardship and Force Majeure in International Commercial Contracts: Dealing with Unforeseen Events in a Changing World, Dossiers of the ICC Institute of World Business Law, Volume 17*, (Kluwer Law International; ICC 2018) 161.

the EU.<sup>21</sup> Since Russia is a permanent member of the UN Security Council, it is unlikely that any anti-Russian sanctions could be adopted within the UN framework. Likewise, other permanent members of the Security Council include the UK, France and the US; therefore, any Russian counter-sanctions are also likely to remain unilateral. The legal qualification of unilateral sanctions is therefore of particular importance for the sanctions regimes involving Russia, and thus for this paper.

The sanctions imposed by the UN Security Council resolutions are undoubtedly a *legal* requirement and thus must be taken into account by all domestic courts of the UN Member States as well as the international arbitrators as part of the transnational legal order. The application of unilateral sanctions, on the other hand, is a more complex matter. Their applicability can be open to doubt, in particular, where they purport to have an extraterritorial effect.

One such situation arose in the *Sensor* case in 1982 in the Netherlands. The Dutch company Sensor through its affiliated company (also registered in the Netherlands but a subsidiary of the US corporation) agreed to deliver to a French company seismographic equipment for later use in the construction of pipelines in the USSR. The same year, the United States imposed an embargo on exports to the USSR of all oil and gas equipment using components or technologies with the US place of origin. The restriction applied to the supply of equipment to the Soviet Union from third countries; the persons for whom the observance of the embargo was mandatory included subsidiaries of US corporations; the prohibition applied equally to the transfer of equipment to other companies or individuals who planned to pass it on subsequently to the Soviet side.<sup>22</sup> The Dutch company refused to deliver the goods referring to the United States embargo as a *force majeure* event. French buyer applied to the court in the Netherlands requesting an order for specific performance. The Dutch court decided that the laws of the Netherlands govern the contract. The judge noted that even in such a situation, the United States embargo in principle could be considered a *force majeure* event. However, in this case, it was not, because the United States had no jurisdiction to impose extraterritorial sanctions binding European companies.<sup>23</sup>

Outside the situations where a sanction was imposed by a UN Security Council Resolution, or by a country whose substantive law governs the contract in question, the legal characterisation of a foreign prohibition becomes particularly important. Should a foreign unilateral prohibition be considered merely an element of fact (local data),<sup>24</sup> i.e. a real-world circumstance that commercial parties cannot control but which does not have the force of law, for them or for a decision-maker? Under such logic, courts and arbitral tribunals would always have to take into account sanctions as a relevant fact, provided that there is sufficient proof of their existence – the remaining discretion would lie in the assessment of their significance for a dispute at hand. Or should the court or arbitral tribunal consider sanctions a legal requirement, and therefore be empowered to determine their applicability by a conflict of laws approach, and then decide

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<sup>21</sup> M Azaredo da Silveira (n 20) 161-162.

<sup>22</sup> ‘Note: Extraterritorial Subsidiary Jurisdiction’, (1987) 50 Law & Contemp Probs 71, 74.

<sup>23</sup> President District Court, The Hague. 17, September 1982, (1982) 22 International Legal Materials 66.

<sup>24</sup> CJH Brunner, *Force Majeure and Hardship under General Contract Principles: Exemption for Nonperformance in International Arbitration* (Kluwer Law International 2008) 320.

whether the prohibition deserves to be given effect? The former approach has been termed the *datum* approach, and the latter – the ‘legal norm’ approach.<sup>25</sup>

As far as foreign mandatory rules generally are concerned, the difference often appears subtle.<sup>26</sup> However, in the context of unilateral sanctions, particularly where these sanctions are directed against or unsupported by the forum state, or where these sanctions are supported by the forum state but rendered ineffective by the substantive governing law chosen by the parties, the distinction acquires fundamental importance. If the court does not have to apply a foreign prohibition mechanically but has a choice of taking it into account or disregarding it depending on the legal and factual matrix of the case, this arguably represents a more flexible and nuanced solution.

One example of a case where a ‘legal norm’ approach could provide a better solution than the traditional ‘datum’ approach was *Borax* case decided by the German *Bundesgerichtshof* in 1960. The contract between a German seller and a German buyer required delivery of 100 tons of borax. The raw materials for its production had to be imported from the US, and the American export licenses provided that no borax should be shipped into any socialist country. The final destination of borax under this contract was, however, East Germany; both parties were aware of this. At the same time, the German government made a conscious decision to refrain from joining the same policy of embargo in relation to borax. The German Supreme Court decided that the contract in question was immoral as it sought to circumvent a binding foreign prohibition, and therefore null and void. In doing so, the court felt bound to consider the American measure in question, and thus effectively enforced the US prohibition of which the state of the forum, the German government, did not approve.<sup>27</sup>

It has been argued that the classification of a foreign mandatory rule or prohibition as a fact or legal rule is of primary significance when the validity of a contract is in question, in particular where the court or arbitral tribunal are faced with the parties trying to circumvent an otherwise applicable requirement through choice of substantive law, choice of forum or other similar means. Where the prohibition in question arose only later, during the performance of the contract, this prohibition can usually be safely treated as a factual circumstance without the need to determine its legal applicability.<sup>28</sup> Indeed, a foreign export ban does not become any less of a problem if a party considers this ban illegal or inapplicable. It is quite enough that the relevant customs authorities are happy to apply the prohibition and thus, as a matter of fact, refuse clearance for the shipment.

It is not clear whether the above distinction ought to be accepted as a universal rule. It has been suggested that, at least in theory, the ‘legal norm’ approach could still provide a better solution.<sup>29</sup> Often though, in disputes involving sanctions as an impediment to performance (*see* section 4.2 below), both approaches would lead to essentially the same result.

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<sup>25</sup> M Azaredo da Silveira, *Trade Sanctions and International Sales* (Kluwer 2014) 35-59; P Mayer, ‘Mandatory Rules of Law in International Arbitration’ 2 *Arb Int* (1986) 274.

<sup>26</sup> GA Bermann, ‘Mandatory Rules of Law in International Arbitration’ in F Ferrari and S Kröll (eds), *Conflict of Laws in International Commercial Arbitration* (JurisNet 2019) 525.

<sup>27</sup> F Vischer, *General Course on Private International Law* (1992-I) 232 *Recueil des Cours* 4, 165.

<sup>28</sup> CJH Brunner (n 24) 168; A Barraclough and J Waincymer, ‘Mandatory Rules of Law in International Commercial Arbitration’, 6 *Melb J Int'l L* 206 (2005) 217.

<sup>29</sup> M Azaredo da Silveira (n 25) 47-48.



### 3. Applicability of Economic Sanctions in Private Disputes

Before going on to consider the effect of sanctions on the performance of private contractual bargains, it is necessary to define the circumstances under which the courts and arbitral tribunals can take into account the prohibitions imposed by a sanctions regime.

In the conditions of an ongoing stand-off between Russia and the West, it is particularly important for the decision-maker to start by determining the relationship between the law of the sanctioning state and the dispute at hand.<sup>30</sup> This relationship may fall into one of the four categories. First, the sanction may form part of the applicable substantive law. Second, it may be binding under the law of the judicial forum or arbitral seat. Third, it may be imposed by the law of the country where contractual performance should take place. Finally, it can fall into none of the three categories above, but still have some connection with the dispute at hand.

Naturally, a Russian court hearing a case that arose from a contract governed by Russian law would not hesitate to apply the Russian counter-sanctions. Likewise, a German court would undoubtedly apply an EU sanction in a dispute governed by German law. However, how exactly could a Russian court take into account the EU sanctions against Russia? What if an arbitral tribunal seated in a European country that refused to accede to the sanction regime against Russia (such as Bosnia and Herzegovina)<sup>31</sup> were to resolve a dispute involving a transaction prohibited by the EU sanctions – should those sanctions apply in this case? These and other questions call for a resolution that relies on the framework of private international law.

If the decision-maker adopts a *datum* approach and treats the sanction as merely a fact, the subsequent discussion need not apply. However, a ‘legal norm’ approach requires further analysis of the same kind as the one applicable to other mandatory rules of law.

The important starting point of this analysis is the characterisation of unilateral sanctions as mandatory rules. There can be little doubt that these prohibitions are indeed mandatory; perhaps they also have a heightened status among the body of mandatory rules since they typically purport to address a worthy (foreign policy) objective, and apply regardless of whatever law governs the particular transaction. Beyond that, however, it is relatively difficult to identify any international consensus as to what should such rules be termed and what exactly are the consequences of the rule’s classification within this category. Such mandatory rules have been variously termed peremptory norms, internationally mandatory rules, ‘*lois de police*,’ rules of immediate application, ‘*lois d’application necessaire*,’ overriding statutes, self-limiting rules and spatially conditioned rules.<sup>32</sup>

The purpose of such mandatory rules has been twofold. First, they vest the national courts with an authority, when they have to apply foreign law, to correct the imbalances produced by the parties’ unequal bargaining power. Second, such mandatory rules empower the courts to

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<sup>30</sup> M Azaredo da Silveira (n 25) 106-126; T Szabados, ‘EU Economic Sanctions in Arbitration’, 35 *Journal of International Arbitration* 4 (2018) 439.

<sup>31</sup> Sarajevo Times, ‘BH Has Not Joined EU’s Sanctions against Russia’ (16 August 2019) <<https://www.sarajevotimes.com/bih-has-not-joined-eus-sanctions-against-russia>> accessed 15 December 2019.

<sup>32</sup> TG Guedj, ‘The Theory of the *Lois de Police*, A Functional Trend in Continental Private International Law – A Comparative Analysis with Modern American Theories’ 39 *Am J Comp L* 661 (1991) 664.

support the important regulatory and policy goals of other nations.<sup>33</sup> For the present purposes, it is the second goal that matters most; but perhaps due to the situations akin to the sanctions stand-off between Russia and the West, it has been observed that, on a global scale, the doctrine has not evolved substantially. No pattern of assistance to foreign interests has emerged.<sup>34</sup>

The general rule applicable in the US on this matter can be found in §187 of the Restatement (Second) of Conflict of Laws, which provides in relevant part:

“(2) The law of the state chosen by the parties to govern their contractual rights and duties will be applied, even if the particular issue is one which the parties could not have resolved by an explicit provision in their agreement directed to that issue, unless...

(b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state in the determination of the particular issue and which, under the rule of §188, would be the state of the applicable law in the absence of an effective choice of law by the parties.”

In the European legal tradition, it is most common to refer to such rules as ‘overriding mandatory rules’ or ‘overriding mandatory provisions.’ An overriding mandatory rule is a rule purporting to address an essential need and thus declaring itself applicable to all situations falling within its purview, regardless of the applicable law.<sup>35</sup> This concept has been dealt with in the Rome I Regulation, the governing text which applies for all EU Member States except Denmark in relation to the choice of law in the contracts concluded after 17 December 2009.<sup>36</sup> Art 9 of the Rome I Regulation contains the following definition:

“Overriding mandatory provisions are provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as its political, social or economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable to the contract under this Regulation”.

Arguably, sanctions regulations fall squarely into this definition. There may remain some room for debate here; however, the majority of experts who wrote on the subject agree with this proposition,<sup>37</sup> thus treating them as overriding mandatory provisions of domestic or EU law.

Therefore, the conditions laid down in arts 9(2) and 9(3) of the Rome I Regulation will determine the application of sanctions regulations by domestic courts of the EU Member States. According to art 9(2), “*nothing in this Regulation shall restrict the application of the overriding mandatory provisions of the law of the forum.*” It means that, regardless of the law governing a contractual relationship, a domestic court of an EU Member State can apply an EU sanction

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<sup>33</sup> HL Buxbaum, ‘Mandatory Rules in Civil Litigation: Status of the Doctrine Post-Globalisation’ in GA Bermann and LA Mistelis, *Mandatory Rules in International Arbitration* (Juris 2011) 33-34.

<sup>34</sup> Ibid 36.

<sup>35</sup> M Azaredo da Silveira (n 25) 50-51.

<sup>36</sup> Art 28 of the Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) OJ L 177, 4.7.2008.

<sup>37</sup> C Kessedjian, ‘Mandatory Rules of Law in International Arbitration: What Are Mandatory Rules?’ 18 *American Review of International Arbitration* (2007) 147, 148; P Mayer (n 25) 272; B Audit, ‘How Do Mandatory Rules of Law Function in International Civil Litigation?’ in GA Bermann and LA Mistelis, *Mandatory Rules in International Arbitration* (Juris 2011) 54.

as an overriding mandatory provision even if the governing substantive law does not endorse the relevant sanctions programme.

Similarly, a national court can disregard a foreign sanction imposed by the governing law if giving it effect would be contrary to the forum's public policy. This conclusion follows from art 9(2) in conjunction with art 21 of the Rome I Regulation, which provides that application of a provision of the law of a third country may be refused if such application is manifestly incompatible with the public policy (*ordre public*) of the forum.

Art 9(3) of the Rome I Regulation lays down an important rule governing the application of the law of a third country, i.e. a country other than that of the forum or that whose substantive law governs the contract. It provides as follows:

“Effect may be given to the overriding mandatory provisions of the law of the country where the obligations arising out of the contract have to be or have been performed, in so far as those overriding mandatory provisions render the performance of the contract unlawful. In considering whether to give effect to those provisions, regard shall be had to their nature and purpose and to the consequences of their application or non-application.”

This provision lays down a three-stage test to determine whether a court could give effect to a foreign sanction as an overriding mandatory provision of a third state.

First, the court must determine the ethical nature and significance of the policy behind the prohibition in question; this is the so-called ‘application-worthiness’ condition.<sup>38</sup>

Second, the court must establish that a connection exists between the contract in question and the sanctioning country. It is noteworthy that in the 1980 Rome Convention on the Law Applicable to Contractual Obligations (the Rome Convention) which the Rome I Regulation has replaced, the equivalent art 7(1) was identical – with the exception relating to this second stage test. Namely, the Rome Convention required a foreign prohibition to have a ‘close connection’ with the situation at hand, whereas the Rome I Regulation has narrowed down this ‘connection’ criterion to only the situations where some part of the obligation have to be or have been performed in the relevant country.

Finally, art 9(3) of the Rome I Regulation requires the court to assess whether the benefits of giving effect to a sanction outweigh those of refusing to take it into account.<sup>39</sup>

In the case of international arbitration, the criteria for deciding whether to apply a foreign mandatory rule look somewhat differently. This discrepancy arises from the fact that the seat of arbitration is not the same as a forum for a domestic court; an arbitral tribunal owes no allegiance to the state of its seat and is under no legal obligation to uphold its policies.<sup>40</sup>

Arbitration statutes are usually quite liberal in allowing the tribunal to adopt such conflict of law rules as they consider appropriate. For example, art 28(2) of the UNCITRAL Model Law on International Commercial Arbitration provides that, failing any designation by the parties,

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<sup>38</sup> M Blessing, *Introduction to Arbitration - Swiss and International Perspectives* 229 (Swiss Commercial Law Series, vol 10, 1999) 266-267.

<sup>39</sup> M Azaredo da Silveira (n 20) 167.

<sup>40</sup> P Mayer (n 25) 277.

the arbitral tribunal shall apply the law determined by the conflict of laws rules which it considers applicable. The national statutes following the Model Law (including art 28(2) of the Russian International Commercial Arbitration Act 1993) usually adopt this provision *verbatim*, thus giving the tribunal a very wide discretion as to which conflict of rules it can apply – those of a seat of arbitration, those in the substantive law governing the contract, etc. In practice, a wide variety of methods and approaches has been used.<sup>41</sup> Thus, arbitral tribunals have much wider discretion in applying or disapplying any given mandatory rule by virtue of the freedom to select the choice of law method.

As far as sanctions are concerned, the further specific features of arbitral decision-making on their application include the following.

First, whereas national courts in determining the ‘application-worthiness’ of a particular sanctions measure will be guided by the national policies and declarations (*e.g.* the courts within the EU will take into account the decisions of the EU political bodies), the international arbitrators need to be guided by the considerations of international (or transnational) public policy. For example, if a particular purpose of a sanctions regulation is supported by the seat of arbitration but scorned by the entire international community, the tribunal should have the freedom to disregard such a prohibition.<sup>42</sup>

This argument sits quite well with the notions of freedom in decision-making that international arbitrators have traditionally enjoyed. However, in the conditions of competing sanctions regimes and the high foreign policy tension, the task of arbitrators becomes extremely difficult and delicate. For example, giving effect to EU sanctions against Russia imposed in connection with the events in Ukraine would imply that the tribunal is happy to disregard Russian objections as to the events that took place during the conflict and as to their compliance with the public international law. Such a decision would thus imply that Russia and the countries supporting it must not, in this event, be treated as a sufficiently large part of the ‘entire international community’ and their position has no bearing on the notion of transnational public policy. And *vice versa*, refusal to give effect to those sanctions against Russia, in light of many decisions and declarations on the subject by numerous bodies with their seat in Western Europe and North America, can be seen by some as a manifestation of an arbitrator’s misunderstanding of the transnational public policy.

A detailed assessment of underlying other political events would normally fall far outside the subject matter of any commercial arbitration proceedings. In any event, an international arbitral tribunal would not be in the best position to assess the facts and contentions of Russia and the sanctioning states concerning the hotly contested matters of fact. There is a risk, therefore, that the arbitrator’s personal political views, their preferred mass media outlets, their underlying assumptions, might influence their assessment of what transnational public policy implies under these circumstances. To author’s knowledge, the problem of political bias has not yet arisen in this form in any set-aside or enforcement proceedings – but if the political tension continues, it is bound to arise sooner or later, and it will be quite interesting to see how it may be resolved.

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<sup>41</sup> AN Zhiltsov, for example, described five different approaches, all of which that were adopted by international arbitral awards. *See* А.Н. Жильцов, ‘Императивные нормы в международном коммерческом арбитраже’ *Международный коммерческий арбитраж* (2004) No 2 16 [AN Zhiltsov, ‘Mandatory Rules in International Commercial Arbitration’, *International Commercial Arbitration Journal* (2004) No 2 16].

<sup>42</sup> M Azaredo da Silveira (n 20) 167-168.

Second, arbitral tribunals, unlike national courts, are not directly bound by provisions such as art 9(3) of the Rome I Regulation. However, the principles on which art 9(3) relies are sufficiently well-recognised, so in the exercise of their broad discretion tribunals can be guided if not by the strict wording then by its underlying rationale. It has been suggested on this basis that the close connection requirement, the second limb of art 9(3) test, can be applied in arbitration more liberally and need not be limited to circumstances where some part of the obligations arising from a contract has been or should be performed in a sanctioning state.<sup>43</sup> In effect, this brings the applicable test away from the current Rome I Regulation and back to that in art 7(1) of the Rome Convention.

One other difference between the approaches of courts and arbitral tribunals that may have practical significance lies in the tribunal's obligation to produce an enforceable award, at the seat of arbitration and otherwise.<sup>44</sup> The New York Convention 1958 treats violations of public policy – though not necessarily every breach of a mandatory rule – as a ground for refusing enforcement. Arguably then, where the tribunal is aware of the place where the eventual award is apt to be brought for enforcement,<sup>45</sup> it is part of the arbitrators' duties to make sure that no such obvious grounds for refusal of recognition and enforcement of an award as a manifest disregard of the enforcement state's overriding mandatory rules are present in the award. Knowing the political stance of the relevant countries on the issue of sanctions and their legitimacy might thus assist the tribunal in arriving at a more balanced and less subjective view.

Turning now to the position in Russian law, it must be pointed out that the statutory regulation of the matter is remarkably similar to the European model discussed above. Art 1192 of the Civil Code (part 3) entitled 'Rules of direct application' reads as follows:

“1. The rules in this Part do not affect the effect of those mandatory rules of the legislation of the Russian Federation, which, due to the indication in the mandatory rules themselves or because of their special significance, including the need to ensure the protected rights and interests of the participants of civil turnover, regulate the relevant relations regardless of the law applicable to them (rules of direct application).

2. When applying the law of a country in accordance with the rules of this Part, a court may take into account mandatory rules of law of another country which is closely connected with the relationship, if according to the law of that country such rules are the rules of direct application. In doing so, the court must take into account the purpose and nature of such rules, as well as the consequences of their application or non-application.”

Thus, despite some difference in terminology (Russian law operates with the term 'rules of direct application' instead of 'overriding mandatory provisions'), the similarities are striking. The definition of what constitutes a rule of direct application is very close to its European counterpart. Likewise, the application of the third country's law is subject to the same three-stage test: 'application-worthiness', close connection and the effects of application or non-application of a foreign rule.

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<sup>43</sup> *ibid* 169.

<sup>44</sup> *See eg* art 42 of the ICC Rules of Arbitration (2017) and art 32 of the LCIA Arbitration Rules (2014).

<sup>45</sup> GA Bermann (n 26) 521.

Furthermore, art 1193 of the Civil Code entitled ‘Public policy reservation’ provides the following:

“The rule of foreign law to be applied in accordance with the rules of this Part does not apply in exceptional cases when the consequences of its application would clearly contradict the fundamental requirements of the rule of law (public policy) of the Russian Federation, taking into account the nature of relations involving a foreign element. In this case, if necessary, the corresponding rule of Russian law must be applied.

A refusal to apply a rule of foreign law cannot be based solely on the difference between the legal, political or economic system of the corresponding foreign state from the legal, political or economic system of the Russian Federation.”

This provision is equivalent to art 21 of the Rome I Regulation.

The judgments of Russian courts applying the above provisions in relation to sanctions and providing a lengthy satisfying rationale for their decision are relatively difficult to come by. However, some interesting positions did emerge during the five years since the beginning of the current sanctions stand-off.

A selective review of the first instance commercial courts’ rulings and decisions rendered in 2019<sup>46</sup> shows that the EU sanctions do feature regularly in contractual disputes resolved by Russian domestic courts. In the vast majority of cases, the courts did not concern themselves with determining the applicability or non-applicability of the EU sanctions in Russia as a matter of Russian law. They did, at the same time, consider the EU economic sanctions against Russia as a ground that may, in principle, excuse the non-performance of contracts requiring the import of affected products into Russia from the EU Member States.<sup>47</sup> This supports the hypothesis that, at least in this category of cases, the Russian courts considered the EU sanctions against Russia as a *datum*, i.e. a factual circumstance that does not require any consideration of the applicability of the relevant EU rules on the territory of Russian Federation.

At the same time, in some notable cases, the courts did engage in such analysis. In assessing the legitimacy of the parallel import, the Constitutional Court of the Russian Federation indicated that the courts can deny legal protection to trademark owners who fail to behave in good faith. The court decided that where a trademark owner complied with the regime of sanctions against Russia and its business entities established by a country outside the proper international legal framework and in contradiction to multilateral international treaties, and as

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<sup>46</sup> This brief review was conducted via the ‘Electronic arbiter’ (arbitr.ru) system, the official e-justice solution of Russian commercial courts. Two reservations about this exercise are due here. First, the decisions and rulings of the first instance courts in Russia do not have any force of a precedent. It is their preponderance and similarity rather than binding force that makes the analysis informative. Second, due to resource limitations, only a narrow category of relevant court decisions had been analysed, namely those rendered in 2019 and mentioning the Council Regulation (EU) No 833/2014 of 31 July 2014 concerning restrictive measures in view of Russia’s actions destabilising the situation in Ukraine OJ L 229, 31.7.2014. It is the author’s hope that a more comprehensive review may be conducted in the future. The brief review did, however, satisfy the needs of this paper by providing some relevant insights.

<sup>47</sup> See, in particular, the Decision of the Commercial Court of the City of Moscow of 8 October 2019, case No A40-103937/2019; the Decision of the Commercial Court of the City of Moscow of 29 April 2019, case No A40-41342/2019; the Decision of the Commercial Court of the City of Moscow of 30 May 2019, case No A40-51145/2019.

a result, this trademark owner took a certain position in relation to the Russian market, it can in itself be regarded as behaviour incompatible with the requirements of good faith.<sup>48</sup>

Another important decision resulted from one of the most widely publicised disputes involving sanctions against Russia over the last few years, both covered in mass media<sup>49</sup> and discussed among the legal experts.<sup>50</sup> In this case, the Siemens's Russian subsidiary agreed to deliver four turbines to the Russian buyer *Technopromexport* for the use in the territory of the Russian Federation. The EU sanctions prohibited the import of energy equipment into Crimea. In the 2015 contract, the buyer guaranteed that the turbines would not be used in Crimea, and their destination would be elsewhere in Russia. However, the media later reported that the initially envisioned construction project never went ahead, and the turbines ended up in the territory of Crimea.

Alleging misrepresentation (in the terminology of Russian law, 'deceit' - art 179 of the Civil Code), the seller sought from the court a declaration that the contract was for this reason null and void, and an order for *Technopromexport* to return the turbines. The court refused to do so and ruled in favour of the defendants. Among other things, the first instance judge pointed out that taking into account the EU sanctions against Russia in this context would be contrary to the forum state's public policy. According to the court, the fulfilment by Russian legal entities in the territory of the Russian Federation of restrictions and prohibitions (embargoes) imposed by the European Union (an international organization of which the Russian Federation is not a member) directly contradicts the fundamental requirements of the rule of law (public policy) of the Russian Federation and damages the sovereignty of the state.<sup>51</sup> The reasoning of the higher courts on appeal was less direct, but nevertheless, they indicated their agreement and refused to allow the Siemens's appeal.<sup>52</sup> Thus, in the context of a claim seeking to declare the contract null and void, the 'legal norm' approach – in its relatively simple form, i.e. applying the public policy exception to foreign sanctions directed against the forum state – has indeed been adopted by a Russian court.

#### 4. The Impact of Sanctions on Contractual Relations

Since it is the domestic law that determines the consequences of the economic sanctions, their impact on contractual relations will also be different in every specific jurisdiction. For every

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<sup>48</sup> Decision of the Constitutional Court of February 13, 2018 No 8-P. It must be noted that the legal positions of the Constitutional Court are binding on all the courts within the Russian judicial system. They do, however, occasionally get distinguished or simply forgotten about if the case for their application has not been duly pleaded before the judge.

<sup>49</sup> Н. Скорлыгина, Е. Черненко, Д. Козлов, И. Сафронов, 'Турбины дали реверс. Под санкции ЕС попали новые компании и чиновники Минэнерго' [N. Skorlygina, E. Chernenko, D. Kozlov, I. Safronov, 'The Turbines Reverse. New Companies and Ministry of Energy Officials Fall Under the EU Sanctions'] (15 August 2017) <<https://www.kommersant.ru/doc/3377458>> accessed 15 December 2019.

<sup>50</sup> С. Гландин, 'Турбины Siemens в Крыму // Суверенитет Украины важнее законов военного времени, решил Суд ЕС' [S. Glandin, 'Siemens Turbines in Crimea. Sovereignty of Ukraine is More Important than the Wartime Laws, Decides the EU Court of Justice'] (13 December 2019) <[https://zakon.ru/blog/2019/12/13/turbiny\\_siemens\\_v\\_krymu\\_suverenitet\\_ukrainy\\_vazhnee\\_zakonov\\_voennogo\\_vremeni\\_reшил\\_sud\\_es#\\_ftn1](https://zakon.ru/blog/2019/12/13/turbiny_siemens_v_krymu_suverenitet_ukrainy_vazhnee_zakonov_voennogo_vremeni_reшил_sud_es#_ftn1)> accessed 15 December 2019; М. Дораев, 'Топ-5 интересных судебных позиций по экономическим санкциям' [M. Doraev, 'Top 5 Interesting Judicial Pronouncements on Economic Sanctions'] (24 February 2018) <[https://zakon.ru/blog/2018/2/24/top-5\\_interesnyh\\_sudebnyh\\_pozicij\\_po\\_ekonomicheskim\\_sankciyam](https://zakon.ru/blog/2018/2/24/top-5_interesnyh_sudebnyh_pozicij_po_ekonomicheskim_sankciyam)> accessed 15 December 2019.

<sup>51</sup> The Decision of the Commercial Court of the City of Moscow of 17 January 2018, case No A40-171207/2017.

<sup>52</sup> The case culminated with the Ruling of the Supreme Court of 15 October 2018 No 305-EC18-16082.

sanctions regime or prohibition, a court or arbitral tribunal cannot consider them in the abstract; rather, a qualification under the applicable contractual provision or the governing law is necessary.

With regard to Russian law, an ICAC at the RF CCI<sup>53</sup> arbitral tribunal brought this point home very powerfully while considering the effects of the new tax legislation on the parties' relations and the correct form of remedy that the claimant could have sought under such circumstances. According to the tribunal, in any event, the influence of new public laws on a private contract can only manifest in those legal forms that are expressly provided for by civil law: invalidating a transaction under art 168 of the Civil Code, termination of an obligation according to art 417 of the Civil Code, amendment or termination of the contract due to a significant change in circumstances according to art 451 of the Civil Code, release of the debtor from liability due to occurrence of *force majeure* events under art 401 of the Civil Code of the Russian Federation.<sup>54</sup>

Two major effects that economic sanctions can have on the parties' contractual relations are the invalidity of the contract and the impossibility of its performance. For the occurrence of each of these effects, a certain range of circumstances must be in place. The following two subsections will consider these effects in turn.

#### 4.1. Invalidity of Contracts

For the contract to be annulled on this ground, first, the parties should have entered into the contract after the enactment of sanctions. Second, sanctions should be legally applicable to the contract.

National legislation in many countries specifies that a contradiction to the law is a sufficient basis to render the contract null and void. For example, in Switzerland, the contract may be declared invalid under art 20 (1) of the Code of Obligations, which stipulates that a contract shall be void if its terms are impossible, unlawful or immoral. This effect occurs, for example, if the contract provides for the supply of goods prohibited by the act imposing sanctions, or the transfer of money to the person from the relevant 'blacklist'. In this case, the contract will only be invalid when the statutory enactment expressly states that transactions which contravene its requirements will be void, or when the object and purpose of such a prohibition require such an effect as the nullity of the contract.<sup>55</sup> For instance, in 1968 the Zurich Commercial Court held contrary to good morals and thus null and void a contract where the parties agreed to smuggle goods in breach of Italian law.<sup>56</sup>

In the US, the courts will refuse to enforce a contract concluded in breach of the law. As in Switzerland, not every contradiction to the law will be considered a sufficient ground for doing

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<sup>53</sup> International Commercial Arbitration Court at the Chamber of Commerce and Industry of the Russian Federation, the leading Russian arbitral institution.

<sup>54</sup> ICAC at the RF CCI arbitral award of 29 April 2008, case No 22/2007. Text of the award is available in: *Практика МКАС при ТПП РФ: 2004 – 2016: К 85-летию МКАС (на основе анонимизированных материалов из журналов «Международный коммерческий арбитраж» и «Вестник международного коммерческого арбитража»)* / Науч. ред. и сост.: А.Н. Жильцов, А.И. Муранов. М., 2017. С. 571 [A.N. Zhiltsov, A.I. Muranov (eds), *Practice of the ICAC at the RF CCI: 2004 - 2016: On the occasion of the 85th anniversary of the ICAC (based on anonymous materials from the journals "International Commercial Arbitration" and "Bulletin of International Commercial Arbitration")* (Moscow, 2017) 571].

<sup>55</sup> E Geisinger (n 15) 410.

<sup>56</sup> RSJ (1968) 354.



so. The court always has a possibility in its sole discretion to provide judicial protection to the contract which, despite a formal violation of the law, does not expressly provide for the commission of prohibited actions. In *Bassidji v Simon Soul Sun Goe*<sup>57</sup> the Court of Appeals for the Ninth Circuit held as follows:

‘... whatever flexibility may otherwise exist with regard to the enforcement of ‘illegal’ contracts, courts will not order a party to a contract to perform an act that is in direct violation of a positive law directive, even if that party has agreed, for consideration, to perform that act.’<sup>58</sup>

In England, the illegality of a contract generally makes it unenforceable. The illegality can arise either by operation of statute or the common law.<sup>59</sup> Where the contract itself is not expressly prohibited by statute, the court has to perform a balancing exercise: the issue is whether public policy requires that a contract should not be enforced because it is tainted with illegality. The notion of public policy has been criticised in England for its vagueness.<sup>60</sup> However, it remains a powerful mechanism for ensuring that the contracts are not misused to contravene the principles of law and statutory prohibition.<sup>61</sup>

In Russia, art 168(1) of the Civil Code makes the transactions violating the requirements of the law or other legal act voidable, which means that they become invalid only if and when a court declares them to be null and void. However, according to Part 2 of the same article, “*a transaction that violates the requirements of the law or other legal act and thus infringes upon public interests or the rights and legitimate interests of third parties is void.*” This rule is subject to a caveat that even in a latter case the law may directly specify that such a transaction is voidable, or provide for other consequences of the violation of the law other than the invalidity of the transaction. This distinction between voidable and void transactions (contracts) is important for Russian law and is known in other countries as well.<sup>62</sup>

Another ground that could be applied to the invalidity of contracts that contravene a sanctions regime is art 169 of the Civil Code of the Russian Federation. According to this article, a transaction made for a purpose that is obviously contrary to the foundations of law and order or morality is void. In cases provided for by law, the court may confiscate in favour of the Russian Federation everything received on such a transaction by parties who acted intentionally, or apply such other consequences as established by law.

At the time of writing, there is still very little published case law involving Russian courts dealing with the civil-law consequences of Russia’s own sanctions. The vast majority of litigation pertaining to the export prohibitions enacted by Russia in 2014 seems to revolve around the administrative relations between the importers of goods and customs authorities – which is not in itself surprising, given that the prohibition of import was chronologically the first measure among the recent counter-sanction regulations. It remains unclear, in particular, whether the Russian courts would treat a transaction made, for example, in violation of the

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<sup>57</sup> *Massoud Bassidji v Simon Soul Sun GOE*. United States Court of Appeals, Ninth Circuit. 15 June 2005, 413 F.3d 928.

<sup>58</sup> *ibid* 936; E Geisinger (n 15) 414.

<sup>59</sup> *Chitty on Contracts* (33rd edn, 2018, 16-005).

<sup>60</sup> *Janson v Driefontein Consolidated Mines Ltd* [1902] A.C. 484, 500, per Lord Davey.

<sup>61</sup> *Enderby Town Football Club Ltd v The Football Association Ltd* [1971] Ch. 591.

<sup>62</sup> Jesse A. Schaefer, ‘Beyond a Definition: Understanding the Nature of Void and Voidable Contracts’ 33 *Campbell L Rev* 193 (2010).

above-mentioned Presidential Decree №560 of 6 August 2014 ‘On the application of certain special economic measures to ensure the security of the Russian Federation’, as voidable or void. Resolution of this issue will depend on the position of the court as to whether the contract which violates the said Presidential Decree would also infringe on the public interests (art 168 of the Civil Code).

The notion of ‘public interest’, in turn, requires additional interpretation. Some authors believe that the expression ‘public interest’ in art 168 of the Civil Code includes the interests of the Russian Federation, its regional governments, municipalities, and the interests of an indefinite number of persons.<sup>63</sup> Other researchers point out that not every concern of a public authority is properly a public interest. For example, when a statute or another legal act aims to cater to the needs of a particular business community and not those of society as a whole, one cannot equate the government’s interest in the enforcement of such regulation with the public interest.<sup>64</sup>

Paragraph 75 of the Supreme Court of the Russian Federation Plenum Resolution of 23 June 2015 №25 ‘On the application by the courts of some provisions of Section I of Part I of the Civil Code of the Russian Federation’ contains the following proposition. In arts 166 and 168 of the Civil Code, the notion of ‘public interest’ includes, in particular, the interests of an indefinite number of people, matters related to public safety and public health, as well as defence, security, and protection of the environment. Transactions which contravene an express prohibition of the law are null and void because they infringe on the public interest. This rule applies, for example, to a pledge or an assignment of claims which are inextricably linked with the creditor’s personality (art 336(1), art 383 of the Civil Code), and insurance of illegal interests (art 928 of the Civil Code). In itself, a discrepancy between the contract and the rules of law, or a violation of the rights of a public authority, does not mean that there is an infringement of the public interest.

There is no doubt that the conclusion of a contract in breach of the Presidential Decree mentioned above should render the contract invalid. As a matter of principle, it seems more logical to consider such a contract voidable so that the court in each case would have an opportunity to assess all the circumstances of the case, the motives of the parties, the information available at the moment when the parties signed the agreement, and so on. This position, in turn, would have to be based on a narrow interpretation of the concept of ‘public interest’ in art 168(2) of the Civil Code which would exclude Russia's foreign policy interests. Given the wording of the above position by the Supreme Court, it seems more likely that a Russian court would consider such contract to be void and not voidable; perhaps it may go as

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<sup>63</sup> Н.А. Агешкина и др. ‘Комментарий к Гражданскому кодексу Российской Федерации. Часть первая от 30 ноября 1994 г. № 51-ФЗ (постатейный)’ (Подготовлен для системы КонсультантПлюс, 2014). Комментарий к статье 168. [NA Agheshkina and others, ‘Commentary to the Civil Code of the Russian Federation. Part One of 30 November 1994 N 51-FZ (clause by clause)’ (Prepared for Consultant Plus, 2014). Commentary to Article 168].

<sup>64</sup> Е.А. Суханов, ‘О частных и публичных интересах в развитии корпоративного права’ (2013) No 1 Журнал российского права 5 [EA Sukhanov, ‘On private and public interests in corporate development’ (2013) No 1 Journal of Russian law 5]; В.А. Степанченко ‘Иностранные инвестиции и торговая политика членов ВТО в рамках Соглашения по инвестиционным мерам, связанным с торговлей’ // Право Всемирной торговой организации: влияние на экономику и законодательство государств Европейско-Азиатского региона (отв. ред. В.Д. Перевалов) (М.: Статут, 2014). [VA Stepanchenko, ‘Foreign investment and trade policies of WTO Members under the Agreement on investment measures related to trade’ in VD Perevalov (ed) ‘The law of the World Trade Organization: the impact on the economy and legislation of the European-Asian region’ (Moscow, Statut, 2014)].

far as to apply art 169 of the Civil Code, opening the possibility of confiscation of the contract's object and proceeds in favour of the Russian Federation. In arbitral proceedings where the substantive law of Russia governs the merits of a dispute the tribunal, of course, will have more freedom in the interpretation of these provisions.

The impact of economic sanctions enacted before the conclusion of the contract but not forming part of the applicable law is not as straightforward. Theoretically, if there is a sufficient connection between the object of the contract and the parties' obligations, and the country which adopted the economic sanctions, the court or the arbitral tribunal may also conclude that a contract is invalid and refuse to enforce it. The relevant considerations that govern the court's decision in such circumstances have been discussed in more detail in section 3 above, but deserve additional comment in this specific context of sanctions regulations as a ground to declare a contract null and void.

To take one international example, in the English case *Regazzoni v Sethia*, the contract between the parties was for the sale and delivery of jute bags from India to Italy for their subsequent resale in South Africa. Parties at the time of contracting knew that the export of jute to South Africa was illegal under the Indian laws; the English law governed the contractual relationship. The seller refused to perform the contract, and the buyer sought damages. The House of Lords decided that the contract was unenforceable and the buyer could not recover damages where the agreement was contrary to the law of a friendly and foreign State. This conclusion had its roots in considerations of public policy and international comity. As Viscount Simonds pointed out in his speech in the House of Lords, an English court will not entertain a suit by a foreign State to enforce its laws of a penal, revenue or political character. It is, on the other hand, nothing else than comity to refuse as a matter of public policy to enforce or to award damages for the breach of, a contract which involves the violation of foreign law on foreign soil.<sup>65</sup>

Professor Hans van Houtte argues that arbitral tribunals can apply directly the economic sanctions which do not form a part of the proper law of the contract under three conditions. First, the sanctions have to consider themselves applicable to the case under the wording of the relevant legal instrument. Second, there must be a sufficient jurisdictional link between the economic sanctions and the transaction. Finally, arbitrators should only take sanctions into account if they deem it appropriate after consideration of all the elements of the case.<sup>66</sup>

It is hard to dispute that the restrictive measures originating in the relevant decision of the UN Security Council must be applied to contracts, even if the government of the target country attempts to neutralise their effect through its domestic law - as Iraq did in 1990.<sup>67</sup> In this case, one could argue that given the hierarchy of the law, the UN sanctions constitute a part of Iraqi law as international peremptory norms, and the compliance with them remains an international legal obligation of Iraq despite the adoption of conflicting domestic legislation.

The possibility that noncompliance with other types of economic sanctions, i.e. those which are not based on the UN Charter and do not form a part of the proper law of the contract might also lead to the invalidity of the contract is quite controversial. An international arbitral tribunal is likely to view the arguments on the applicability of such sanctions with some scepticism. For example, in *Götaverken* the contract for the supply of three oil tankers between the Swedish seller and the Libyan buyer was governed by Swedish law. The buyer refused to accept the

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<sup>65</sup> *Regazzoni v KC Sethia (1944) Ltd.* [1957] 3 WLR 752, [1958] AC 301 at 318-319.

<sup>66</sup> H van Houtte, 'Trade Sanctions and Arbitration' (1997) 25 *International Business Law* 166, 168.

<sup>67</sup> The 1990 Iraqi law 'On the protection of property rights and interests of Iraq in the country and abroad'.

delivery citing the Libyan boycott extending to all commercial relations with Israel. The arbitral tribunal considered these restrictive measures to be irrelevant for the resolution of the dispute, except to the extent that the contract itself provided for their applicability. The only mention of these sanctions in the agreement was the seller's obligation to provide a certificate confirming that the construction of the ships did not involve the use of materials and equipment manufactured in Israel. The seller provided such a certificate, so the buyer had no grounds for a refusal to perform the contract.<sup>68</sup>

The Russian courts are yet to consider such kind of a situation. However, in view of the discussion above, it seems unlikely that they would be willing to apply unilateral sanctions that do not form part of the proper law of the contract as a ground for declaring the contract invalid. They would almost certainly decline a request to give effect to the sanction regimes directed against Russia as any part of the factual matrix necessary for declaring a contract null and void. This has already been demonstrated in the dispute between Siemens and *Technopromexport*<sup>69</sup> where the plaintiff has unsuccessfully attempted to use the EU sanction against Russia as part of the misrepresentation claim (art 179 of the Civil Code of the Russian Federation). The courts predictably refused to apply those provisions on the grounds of the forum's public policy.<sup>70</sup>

#### 4.2. *Impossibility of Performance*

Ascertaining the impossibility to perform an obligation also requires that two main conditions must be in place: sanctions must enter into force after the conclusion of the contract, and their introduction must indeed constitute an obstacle to its proper performance.

According to art 119 of the Swiss Code of Obligations, an obligation is discharged where its performance became impossible by circumstances for which the debtor cannot be made responsible. The adoption of acts by public authorities that prohibit the actions forming part of the debtor's obligations under the contract, as a rule, falls under this definition of a supervening impossibility. At the same time, there is a condition for the application of this rule, namely that the debtor did not and could not foresee the events which would make it impossible to perform its obligations under the contract. In one of the cases decided in 1985 by the Federal Tribunal, a Swiss company agreed to build and deliver the atomic installation 'Mini 8067' to Pakistan. Subsequently, the Federal Office of Energy imposed a ban on the delivery of a similar installation '8062 Micro', and the seller did not perform its obligation on the ground that it has become impossible to do so under art 119 of the Code. The Federal Tribunal rejected this argument and pointed out that the debtor is responsible for the legal impossibility of performance where he knew or should have known, having investigated the matter with due diligence at the time of conclusion of the contract, that the circumstances preventing the proper performance could arise. In the present case, the adoption of such a ban was foreseeable for the debtor. The provisions of the law give the Federal Office of Energy the right to impose such a ban at any time. Exporter of nuclear technology must always expect that the Federal Council may, due to unforeseen political events in the world, introduce some restrictions in the energy industry.<sup>71</sup>

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<sup>68</sup> *Shipyard, AB Götaverken (Sweden) v Libyan General Maritime Transport Organization (GMTO) (Libya), General National Maritime Transport Company (GMTC) (successor First Defendant) (Libya)* Award in Case Nos. 2977, 2978 and 3033 in 1978, ICC Award No. 2977. Yearbook Commercial Arbitration 1981, 133.

<sup>69</sup> For more details, see above at section 3, the text accompanying notes 52-55.

<sup>70</sup> The Decision of the Commercial Court of the City of Moscow of 17 January 2018, case No A40-171207/2017.

<sup>71</sup> Geisinger (n 15) 416.

In the US, the Uniform Commercial Code (UCC) establishes in §2-615:

“Delay in delivery or non-delivery in whole or in part by a seller ... is not a breach of his duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.”

These provisions of the Uniform Commercial Code were accepted in judicial practice and became known as ‘commercial impracticability’. In *Harriscom Svenska v Harris Corp*,<sup>72</sup> the court applied this doctrine to excuse non-performance of an obligation, even when the relevant government regulation was not formalised in the form of a binding legal act, but constituted merely a recommendation. In this case, it was a recommendation not to supply military equipment to Iran.<sup>73</sup>

In England, supervening illegality is a well-recognised head of frustration, which entails the discharge of a contract, bringing the contract to an end.<sup>74</sup> Where English law governs a contract, it will be discharged by frustration when something occurs after its formation rendering the fulfilment of the contract legally impossible, or transforming the obligation to perform into a radically different obligation.<sup>75</sup> However, where one or even both parties are affected by sanctions, it does not automatically mean that the contract has become frustrated. Where the regulations make it possible for a designated person to request a license from a competent authority to perform an otherwise forbidden operation, such as a transfer of funds, an additional enquiry is in order. In circumstances where the relevant persons did not even apply for a licence, they must satisfy the Court that it was no use attempting to make an application.<sup>76</sup> Thus, the contract will only be frustrated if the relevant party failed to obtain a licence despite the exercise of best endeavours, or if there is proof that the licence was unobtainable in principle.<sup>77</sup>

As a result, English courts have construed the doctrine of frustration narrowly in such cases. For example, summary judgment was granted in favour of an Iranian bank in relation to the fees due from its customer under a facility agreement. The agreement was concluded before the sanctions entered into force and contemplated that it was for the customer to do what was necessary for the performance of the obligations. Since no application was ever made, and in the absence of evidence that such application would not be granted, the court ruled in favour of a sanctioned entity.<sup>78</sup> In another case, the court explained that awarding a sum of money in favour of two sanctioned entities would not constitute a circumvention of the sanctions regulations, because it would merely lead to crediting their frozen accounts – provided those accounts remain frozen.<sup>79</sup>

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<sup>72</sup> *Harriscom Svenska, AB v. Harris Corp.*, 3 F.3d 576 (2d Cir. 1993).

<sup>73</sup> Geisinger (n 15) 418-419.

<sup>74</sup> *Chitty on Contracts* (33rd edn, 2018, 23-022 and 23-024).

<sup>75</sup> *ibid* 23-001.

<sup>76</sup> *Windschuegl (Charles H) v Alexander Pickering & Co* (1950) 84 Ll. L. Rep. 89.

<sup>77</sup> *Malik Co v Central European Trading Agency* [1974] 2 Lloyd's Rep. 279.

<sup>78</sup> *Melli Bank v Holbud* [2013] EWHC 1506 (Comm).

<sup>79</sup> *DVB Bank SE v Shere Shipping Company Limited, Tongham Shipping Company Limited, Uppercourt Shipping Company* [2013] EWHC 2321 (Comm) at [92].

Similarly, art 416 of the Russian Civil Code provides that the subsequent impossibility of performance shall terminate the obligation where it is due to circumstances for which none of the parties is responsible. A specific ground for the termination of obligations is laid down in art 417 of the Civil Code. This article stipulates that where the performance of an obligation becomes impossible in whole or in part as a result of an act by a State or a local authority, the obligation is terminated in whole or in relevant part. Given that the termination under art. 417 of the Civil Code entails the possibility for the contracting parties to recover the resulting damages from the relevant public authority under certain circumstances, it is logical to apply this ground only to the acts of the Russian Federation, its regional government authorities and local authorities. Therefore, in cases where the impossibility of performance is due to the enactment of a restrictive measure by a foreign State, obligations of the parties shall terminate according to art. 416 of the Civil Code and not art. 417.

The general *force majeure* provisions in Russian civil law are contained in art 401 of the Civil Code. According to this article,

“unless otherwise provided by law or contract, a person who has not performed or improperly performed an obligation in the course of entrepreneurial activity shall be liable if he does not prove that proper performance was impossible due to *force majeure*, that is, extraordinary events that were unavoidable under the circumstances. Such events cannot include, in particular, a breach of obligations on the part of the debtor’s other counterparties, the absence on the market of goods necessary for contractual performance, or the debtor’s lack of the necessary funds.”

In the context of public procurement, a Russian commercial court has considered the impossibility of importing the relevant goods as a sufficient ground to refuse the claim for contractual penalties (liquidated damages). In this case, a state psychiatric hospital sought to recover the contractual penalties from its supplier who refused to deliver washing powder relying on the Presidential Decree №560 of 6 August 2014. According to the relevant Russian statute governing the performance of contracts resulting from public procurement, a party does not have to pay the contractual penalties or liquidated damages if the failure to perform was caused by a *force majeure* event.<sup>80</sup> Refusing the claim, the commercial court pointed out that the evidence has supported the conclusion that the import restrictions applied to the goods in question, which constituted the relevant *force majeure* event and made the delivery impossible.<sup>81</sup>

In a similar context, it seems uncontroversial that Russian state courts will consider the contravention to the Russian counter-sanctions regime as a ground to recognise the impossibility of carrying out the prohibited commercial activity. In one of the Intellectual Property Court<sup>82</sup> cases decided in 2018, *Danone Russia* (the plaintiff) requested the Court to cancel the registration of a trademark belonging to *Molkerei Alois Muller GmbH & Co. KG* (the defendant) on the grounds that it was unused in Russia for three consecutive years (2014-2017). While agreeing that *Danone* has established its valid legal interest in contesting the trademark, the court pointed out that, according to art 19 of the TRIPs Agreement, circumstances arising independently of the will of the owner of the trademark which constitute an obstacle to the use of the trademark, such as import restrictions on or other government

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<sup>80</sup> art 34 of the Federal Law ‘On the Contract System in the Procurement of Goods, Works and Services for the State and Municipal Needs’.

<sup>81</sup> Judgment of the Ninth Appeal Court of 21 June 2016, case number A40-6478/2016.

<sup>82</sup> A specialised state court established within the Russian judicial system in 2013.

requirements for goods or services protected by the trademark, shall be recognized as valid reasons for non-use. Since the defendant was a German company, and the Presidential Decree №560 of 6 August 2014 prohibited the importation of milk and dairy products from the EU, the use of defendant's trademark in Russia was impossible during the relevant period. Therefore, the court refused to cancel the trademark and ruled in favour of the defendant.<sup>83</sup>

As noted above, many Russian courts have also considered the EU economic sanctions against Russia as a ground that can excuse the non-performance of contracts requiring the import of affected products into Russia from the EU Member States.<sup>84</sup> Other Russian courts, however, refused to consider the sanctions against Russia as *force majeure*. For example, in 2015 decision of the Eighteenth Commercial Court of Appeal, the court relied on the lack of evidence confirming that the relevant EU sanctions indeed prevented the import of goods into Russian Federation, particularly because the seller's Czech counterparty has eventually overcome this obstacle and performed the delivery, albeit much later than required by the contract.<sup>85</sup> It remained unclear from the text of the decision whether the Czech company has done so by obtaining an authorisation from the competent authorities, which could arguably be relevant for the assessment under art 401 of the Civil Code. In a similar situation, the Commercial Court for the North-Caucasian Circuit declined to consider the EU economic sanctions as a *force majeure* event, explaining (somewhat cryptically) that the imposition of economic sanctions does not in itself indicate that this very circumstance led to the lateness in delivery of goods, and also cannot release of the defendant from the obligation to deliver the goods within the timeframe established by the contract. As in the previous case, the goods in question (industrial equipment) were eventually delivered to their destination in the Russian Federation, albeit with a significant delay; the reasons for the delay, however, were not explained in the decision any further.<sup>86</sup> This demonstrates some inconsistency of court practice on this question but also highlights the extensive number of circumstances the courts should consider when deciding whether the *force majeure* defence is available in every individual case.

The Russian commercial courts have also considered the situations where, due to the nature of the contract and the parties' business, it should have been reasonable for them to take into account the possibility of sanctions. As in Switzerland, this directly affects the feasibility of the *force majeure* defence. In one of the cases of the Commercial Court of the City of Moscow, a buyer sought to recover the contractual penalties due to the failure of the seller to deliver the goods in accordance with the contract. The goods in question included a gas chromatograph-mass spectrometer with a mass analyser to be imported from Germany; the buyer was a government enterprise whose products and activities were mostly of a military character. The German authorities failed to issue an export license required for the timely delivery of the spectrometer, which led to the dispute between the parties. The court took into account that the possibility of the contract being affected by the EU sanctions was reasonably foreseeable for the parties. It also pointed out that, although the goods originated in Germany, the seller's own supplier was another Russian company (an intermediary). Thus the court decided in favour of the plaintiff and recovered the contractual penalties. It did, however, reduce their amount

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<sup>83</sup> The Intellectual Property Court judgment of 26 June 2018, case number SIP-601/2017.

<sup>84</sup> See, in particular, the Decision of the Commercial Court of the City of Moscow of 8 October 2019, case No A40-103937/2019; the Decision of the Commercial Court of the City of Moscow of 29 April 2019, case No A40-41342/2019; the Decision of the Commercial Court of the City of Moscow of 30 May 2019, case No A40-51145/2019.

<sup>85</sup> Judgment of the Eighteenth Appeal Court of 27 November 2015, case number A07-12459/2015.

<sup>86</sup> Judgment of the Commercial Court for the North-Caucasian Circuit of 13 September 2018, case No A53-3447/2018.

substantially on the basis of art 333 of the Russian Civil Code as it considered the originally claimed amount unreasonable and excessive.<sup>87</sup>

It is noteworthy that, for the establishment of the impossibility of contractual performance, it usually does not matter whether the economic sanctions in question were a part of the proper law of the contract. Indeed, to declare the contract void, it is necessary to understand whether the compliance with a government prohibition was legally binding on the parties. Conversely, to determine whether it was impossible to perform the contract, it is more important to understand how significant was the practical effect of this prohibition on the contractual performance. For example, a contract between two Russian companies governed by Russian law may require the parties to carry out some activity in the territory of China. If later on, the Chinese government enacts a regulation expressly prohibiting such activity, there can be no doubt that it will have become legally impossible to perform the obligations (art 416 of the Civil Code).

Thus, in this category of cases, Russian courts, typically, are more likely to follow the *datum* than the ‘legal norm’ approach.<sup>88</sup> Where the remedy that a party seeks is not *force majeure* as an excuse for non-performance but rather an adaptation of contract due to the radical change of circumstances, the position remains the same, although the relative weight and relevance of sanctions may change in line with the requirements of the relevant legal rule.

According to art 451 of the Civil Code of Russian Federation,

“1) A significant change in the circumstances on which the parties relied when concluding the contract shall be the ground for its amendment or termination, unless otherwise provided by the contract or follows from its nature.

2) If the parties have not reached an agreement on bringing the agreement in accordance with significantly changed circumstances or on its termination, the agreement may be terminated or amended by the court at the request of the party, subject to the following conditions:

(1) at the time of conclusion of the contract, the parties proceeded on the assumption that such a change in circumstances would not occur;

(2) the change in circumstances is caused by reasons that the interested party could not overcome after their occurrence with the degree of care and diligence that was required of it by the nature of the contract and the market conditions;

(3) the performance of the contract without changing its terms would so violate the balance of interests of the contracting parties and would entail such damage for the interested party that it would largely lose what it was entitled to expect when concluding the contract;

(4) it does not follow from a custom or nature of the contract that the risk of a change in circumstances is borne by the interested party.”

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<sup>87</sup> The Decision of the Commercial Court of the City of Moscow of 30 May 2019, case No A40-51145/2019.

<sup>88</sup> See above section 2 of this paper.



In a 2017 ruling, the Supreme Court of Russia considered a claim for termination of the contract under art 451 of the Civil Code by the VTB Bank. The Bank relied on the introduction of US, Canadian and EU sanctions against it and the resulting losses it incurred to argue that it became necessary to close a number of branch offices across Russia, making unnecessary the long-term lease contract with the owner of an office in the city of Saransk that the Bank earlier concluded. Reversing the decisions of lower courts that supported the Bank's position, the Supreme Court did not engage in any discussion of the sanctions' applicability in the territory of Russia, but instead ruled as follows. When deciding to close the office located in the disputed premises, the Bank was guided by the considerations of economic feasibility. Entrepreneurial activity implies a risk, which the Bank, being a professional participant of the financial services market, could not ignore when concluding the lease agreement. With due diligence, the Bank, entering into contractual relations on its own initiative, should have foreseen a possibility of such an economic situation. Thus, there were no grounds for terminating the contract under art 451 of the Civil Code. Since the contract did not name the sanctions under its *force majeure* provisions, the contractual grounds for terminating the contract were unavailable as well.<sup>89</sup>

There have been reported cases where a reference to economic sanctions was regarded only as an excuse and not a genuine reason for non-fulfilment of the contractual duties. Thus, in the decision of the Commercial Court of the Sverdlovsk region of 3 April 2015 the parties entered into a contract for the sale of pink salmon which the defendant did not perform. As a reason for non-fulfilment of contractual obligations, the defendant referred to the Presidential Decree №560 of 6 August 2014 'On the application of certain special economic measures to ensure the security of the Russian Federation' and the subsequent Decree of the Russian Government. These legal instruments listed the agricultural products, raw materials and foodstuffs prohibited for import into the territory of the Russian Federation. The consequence of these Russian countermeasures was a significant increase in the price of the fish which the defendant undertook to deliver to the plaintiff. These circumstances were purportedly *force majeure* (unforeseeable and insurmountable) since without making the performance of the contract impossible as such, they significantly increased the cost of purchase of the goods from the manufacturer. The Court rejected this argument, pointing out that according to art 2 (1) of the Civil Code, business activities are carried out independently, at one's own risk, and aim at systematically deriving a profit. Therefore, having entered into a contract with the plaintiff for the supply of frozen fish, the defendant, not being the manufacturer of the product, accepted all possible risks, including that of an increase of the costs.<sup>90</sup>

This is consistent with international practice. For example, in the ICC case 1782/1973,<sup>91</sup> a German and a Yugoslav company signed a contract for the supply and maintenance of trucks in three Arab countries. After these countries introduced sanctions against Israel, it became impossible for the defendant's employees who were Israeli citizens to obtain visas to carry out services under the contract. The respondent submitted that these circumstances amount to *force majeure* and make the performance of the contract impossible. The tribunal rejected this argument, pointing out that it does not explain the 26-month delay in fulfilling the obligations under the contract. As a company, respondent also had the right to hire nationals of other countries to perform the works.

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<sup>89</sup> Ruling of the Supreme Court of the Russian Federation of 23 May 2017 No 301-ES16-18586, case No A39-5782/2015.

<sup>90</sup> The decision of the Commercial Court of Sverdlovsk region of 3 April 2014 in case №A60-825/2015.

<sup>91</sup> ICC award in case No. 1782/1973, JDI 1975, 923-924.

## 5. Conclusion

As shown above, economic sanctions do have a serious impact on the parties' private contractual sphere. Despite the fact that they are a product of foreign policy and altogether a phenomenon of a different order compared to commercial disputes, their influence on private contractual interests is hard to overlook. Legal issues that arise in such interactions are often complex and require careful analysis in every case.

There is no doubt that the sanctions adopted by the UN Security Council resolutions under the UN Charter have greater weight than national laws. Attempts to neutralise such resolutions through the adoption of domestic legislation are unlikely to look persuasive for arbitral tribunals that will take into account the rules of international public policy. The validity of a reference to the UN Security Council restrictive measure as a circumstance entailing the invalidity of the contract or the impossibility of contractual performance, as a rule, will be straightforward for the decision-maker. However, the unilateral sanctions adopted by individual States or groups of States present more complex questions, both in terms of legitimacy and legal validity and as a question of how such measures should be taken into account in the resolution of contractual disputes. Domestic courts and international arbitral tribunals should find out whether they are part of the proper law of the contract; whether any legitimate countermeasures exist in the target State and third countries; whether they conform with the conventional understanding of the limits of the extraterritorial jurisdiction where the sanctions instrument makes such an attempt.

In the current situation of a political stand-off between Russia and the West, ascertaining what exactly should qualify as transnational legal order in relation to sanctions is fraught with difficulties and dangers of political bias for international arbitrators. The position of national courts on this matter is more straightforward, as they are bound to rely on the political pronouncements of their own government. Arbitrators have more flexibility, but any choice must nevertheless be substantiated. This matter certainly deserves additional study, particularly inasmuch as it can influence the determination of circumstances that allow an arbitral tribunal to take into account a unilateral economic sanction of a third country which does not form part of the proper law of contract. In making decisions involving the transnational public policy as a ground for giving effect or refusing to give effect to a particular sanctions regime, arbitral tribunals have to tread very carefully to ensure the enforceability of their awards.

The statutory law in Russia, both in the area of private international law that determines the applicability of sanction regimes and in general contract law, is well-developed. The rules of the Civil Code contain comprehensive regulation on matters such as choice of law, the invalidity of contracts and impediments to contractual performance. In a number of aspects, the Russian statutory regulation is remarkably similar to its European counterparts and has undoubtedly been influenced by the European legal tradition. As far as the economic sanctions are concerned, however, Russia does not have such extensive experience in this field as the EU Member States or the US. As a result, its sanctions regulations are not as mature, and the courts are not as accustomed to deal with the private-law consequences of sanctions.

Although the case law on sanctions remains scarce in Russia, over the five years since 2014, a body of decisions has accumulated. Their brief overview as conducted in this paper produced some interesting insights. The majority of known cases come from the Russian commercial courts – which is not surprising given that the overall number of cases that go to arbitration is much smaller and the arbitral proceedings are confidential. But due to the well-known

advantages of arbitration generally, and particularly due to the features of arbitral decision-making in cases involving sanctions outlined in this paper, there will undoubtedly be more arbitrations dealing with sanctions in the years to come.

The cases involving the application of sanctions as a ground for invalidity of contracts are relatively rare; much more prevalent in Russian courts is the case law dealing with them as an impediment to performance. In resolving those cases, Russian courts have demonstrated that they are usually happy to consider the EU and US sanctions against Russia as factual circumstances, without going deeply into their legal applicability on Russian territory. One area where greater consistency of court practice would be desirable is the determination of whether, and under what conditions, the foreign sanctions constitute a valid defence under art 401 of the Russian Civil Code. In other categories of cases, however, going beyond the *force majeure* defence, the courts are prepared to refuse taking sanctions against Russia into account on the public policy grounds, and even use compliance with foreign sanctions regimes as an important element in the assessment of a commercial party's good faith.

In all these categories of cases, an arbitral tribunal would have a much wider discretion as to the application of relevant rules of contract law and private international law. This freedom has its limits, but it does provide the contracting parties with additional opportunities in the current economic and political climate.