Arbitration: Paris Court Explores the Post-Award Impact of International Sanctions

12 June 2020

On June 3, 2020, the recently created International Chamber of the Paris Court of Appeal rejected an application to set aside an international arbitration award arising out of the termination of a contract between a French company and an Iranian company in the context of economic sanctions against Iran.[1]

This is the Court's second decision regarding international arbitration awards, after the *Dommo* case earlier this year on the topic of arbitrator disclosure (on which we reported here). It provides valuable guidance on the interplay of economic sanctions and arbitration, an area where little contemporary guidance exists.

The Court found that U.S. economic sanctions against Iran do not form part of international public policy, but UN and EU sanctions do. These findings will have important implications for tribunals navigating the law of the seat, the law applicable to the substance of the dispute, and other potentially relevant sources of law. The decision is also timely in light of renewed resistance, in France and elsewhere, to the extraterritorial reach of certain U.S. measures.

The Sofregaz Case. French company Sofregaz had a contract governed by Iranian law with an Iranian company, the Natural Gas Storage Company ("NGSC"), for the conversion of a gas field located in Iran into underground storage. In the course of the project, Sofregaz informed NGSC that banks had refused to extend the bank guarantees necessary under the contract, ostensibly due to various international sanctions against Iran. NGSC terminated the contract, alleging that Sofregaz had breached the contract and delayed the continuation and completion of the project.

In 2014, Sofregaz brought arbitration proceedings against NGSC under the ICC Rules of Arbitration, seated in Paris, for wrongful termination of the contract. In 2018, the tribunal rendered an award in favor of NGSC. In 2019, Sofregaz filed an application to set aside the award before the International Chamber of the Paris Court of Appeal,

[1] Paris Court of Appeal (Chamber 5-16), June 3, 2020, No 19-07261.

largely on the basis that the tribunal allegedly failed to take into account the impact of international sanctions against Iran on the performance of the contract.

On June 3, 2020, the Court rejected the application to set aside the award. The Court found that (*1*) the award did not fall foul of the requirement, in French law and under the ICC Rules, that awards be reasoned, because "arbitrators are not required to follow the parties in the detail of their arguments" and the tribunal had "implicitly but necessarily" considered the international sanctions argument as neither relevant nor necessary to the solution of the dispute; (*2*) the tribunal did not violate international public policy in failing to consider the impact of U.S., UN, and EU economic sanctions against Iran; and (*3*) the tribunal's acceptance of documents and arguments submitted late, to which Sofregaz had not timely objected, did not constitute a violation of due process.

When Do Economic Sanctions Constitute "International Public Policy"? The Court's reasoning with respect to sanctions is perhaps the most notable aspect of the decision. Sofregaz had argued that the tribunal had failed to consider the impact of international sanctions against Iran on the performance of the contract, and thus that its recognition would be contrary to international public policy ("*l'ordre public international*").

French courts define international public policy as "the body of rules and values whose violation the French legal order cannot tolerate, even in the international context."[2] Violation of international public policy is both a basis to set aside an award seated in France and a defense to enforcement of a foreign-seated award.[3]

The Court unequivocally held that the unilateral sanctions taken by U.S. authorities against Iran cannot be regarded as the expression of an international consensus, since the extraterritorial reach of these sanctions is disputed by both the French and EU authorities. Accordingly, the Court concluded that the U.S. sanctions at issue did not form part of French international public policy[4], and that the tribunal's failure to take them into account cannot be a reason to set aside the award.

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[2] *See* para. 47: " . . . l'ensemble des règles et des valeurs dont l'ordre juridique français ne peut souffrir la méconnaissance, même dans des situations à caractère international." Also see for instance Paris Court of Appeal (Chamber 1-1), October 23, 2012, No 11-10023.

[3] Articles 1520 and 1525 of the French Code of Civil Procedure.

[4] *See* para. 67: ". . . les sanctions émanant des autorités américaines contre l'Iran, quand bien même elles auraient vocation à s'appliquer hors le territoire des États-Unis, ne peuvent être rattachées en tant que telles à des règles et valeurs dont la France ne peut souffrir la méconnaissance, et ce faisant ne peuvent être intégrées dans la conception française de l'ordre public international. . . ."

In contrast, the Court held that UN Security Council Resolutions and EU Regulations imposing economic sanctions against Iran[5] would form part of international public policy, since they are intended to contribute to the maintenance or restoration of international peace and security.[6] However, the Court recalled that a violation of international public policy must be "effective" and "concrete" to constitute grounds for set-aside of an award. Courts sometimes also require the breach of international public policy to be "manifest".[7] The Court denied the application for set-aside on this basis, because the UN and EU sanctions at issue did not apply to the Sofregaz contract in the first place.

Arbitration Involving Sanctioned Countries: Between a Rock and a Hard Place? The Court's decision provides welcome guidance for the potential implications of international sanctions on award enforcement.

Economic sanctions can arise at several stages of the arbitral process. Questions may arise as to whether sanctions affect the validity of the arbitration clause and the arbitrability of a dispute, the availability of defenses and excuses for non-performance as a matter of substance, the conduct of parties, arbitrators and institutions in the course of the arbitration, and of course the enforceability of an arbitral award—especially if the laws of the seat, the law of the contract, the laws applicable to the arbitrators, and the enforcing jurisdiction differ with respect to sanctions.

There is little guidance, let alone consensus, on whether economic sanctions constitute part of the public policy of the enforcing State, and if so, whether they outweigh the enforcing State's policy in favor of the finality and enforceability of arbitral awards—especially when arrangements could be made for payment to be made into a blocked account which could be released after sanctions are lifted.[8]

EU Member State courts must apply overriding mandatory provisions of EU law, including economic sanctions imposed by the EU, *ex officio*, even if the parties to the

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5 United Nations Security Council Resolutions 1737 of December 23, 2006, 1747 of March 24, 2007, and 1803 of March 3, 2008; European Union Council Regulations (EC) No 423/2007 of April 19, 2007, (EU) No 961/2010 of October 25, 2010, and (EU) No 267/2012 of March 23, 2012 concerning restrictive measures against Iran.

6 *See* para. 55 about UN Resolutions: ". . . les résolutions précitées, en ce quelles ont pour objet de contribuer au maintien ou au rétablissement de la paix et de la sécurité internationales, portent des règles et des valeurs dont il convient de considérer que l'ordre juridique français ne peut souffrir la méconnaissance, et ce faisant relèvent de la conception française de l'ordre public international." Similar language is used at para. 57 about EU Regulations.

7 For a recent example, see Paris Court of Appeal (Chamber 1-1), June 2, 2020, No 17-17273.

8 *See, e.g., Iran Defense Ministry v Cubic Defense Systems, Inc,* 665 F.3d 1091 (9th Cir. 2011); *Ameropa A.G. v. Havi Ocean Co. LLC*, 2011 WL 570130 (SDNY 2011); *see also Ministry of Defence and Support for Armed Forces of the Islamic Republic of Iran v. International Military Services Ltd* [2020] EWCA Civ. 145.

dispute did not raise their application.[9] The situation with respect to third-State (non-EU) sanctions is less clear. Particular problems can arise when these economic sanctions purport to have extraterritorial reach and conflict with other bodies of law that may be relevant in the context of an arbitration.

Iran is a salient example. The so-called EU "Blocking Regulation" was updated in 2018 to include extraterritorial U.S. sanctions against Iran, and purports to prevent certain EU persons from complying with U.S. secondary sanctions on Iran.[10] The amended Regulation applies to EU persons even in cases where such EU persons have entered into contracts governed by non-EU or non-EU member state laws. Some Member States (like France) have not, so far, instituted penalties for violation of the Blocking Regulation, but others (like Austria) have, and France and other countries also have domestic "blocking statutes" aimed at neutralizing the effect of various foreign measures.

The amended Regulation may thus position EU persons, particularly EU subsidiaries of U.S. companies, that are engaged in commercial dealings involving Iran with the unenviable choice of whether to risk scrutiny by U.S. or EU authorities. It also poses difficult questions for arbitration users. The EU Commission's Guidance Note explains that the Blocking Regulation applies to "arbitration awards" based on the listed measures and "[n]ational authorities . . . including . . . arbiters."[11] Would it violate the Blocking Regulation for an EU national arbitrator to hold that non-performance of a contract is excused on the basis of sanctions that are blocked under the Blocking Regulation? Would an award that gave effect to U.S. sanctions subject to the Blocking Regulation be enforceable in EU Member States?

In practice, parties increasingly have included in their contracts provisions that set out the specific rights and obligations that will be triggered in the event that sanctions affect performance of the contract rather than relying on general principles such as frustration of purpose, force majeure, and impossibility of performance. As we previously reported, at least one court has questioned whether complying with such an express contractual clause would fall foul of the Blocking Regulation (see here)[12]; and

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9 *See, e.g., Ministry of Defence and Support for Armed Forces of the Islamic Republic of Iran v. International Military Services Ltd* [2019] EWHC 1994 (Comm); *cf. also* Case C-126/97, *Eco Swiss China Time Ltd. v. Benetton International NV*, European Court of Justice, Judgment of 1 June 1999.

10 Council Regulation (EC) No 2271/96 of 22 November 1996, amended by Commission Delegated Regulation (EU) 2018/1100 of 6 June 2018.

11 EU Commission "Guidance Note - Questions and Answers: adoption of update of the Blocking Statute" No 2018/C 277 I/03, point 4.

12 *See Mamancochet v. Aegis* [2018] EWHC 2643 (Comm), as upheld on appeal [2020] EWCA Civ. 145.

another decision recently held that a contractual "no claims" clause prevents recovery of interest on an arbitral award during the sanctions period (see here).[13]

In parallel, as we reported last year (see here), debates are unfolding in France and at the EU level about the extraterritorial reach of various U.S. regulations and their application by U.S. authorities. The Court's decision in *Sofregaz* is consistent with the view that unilateral U.S. sanctions should have little weight on French soil.

This is a highly complex area, involving the intersection and even direct conflict of national, supranational and international law, with potentially serious consequences for making missteps. It involves not only regulatory compliance in existing arrangements but also taking account of these evolving issues in new contracts. If you require advice or guidance, we remain ready to assist.

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Please do not hesitate to contact us with any questions.


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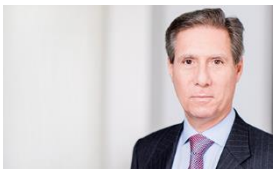
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[13] *See Ministry of Defence and Support for Armed Forces of the Islamic Republic of Iran v. International Military Services Ltd* [2019] EWHC 1994 (Comm).

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