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Arbitration & Litigation

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Dear reader,

In this issue of our Quarterly Update Arbitration & Litigation, you will find once more reports on current topics and developments in the field of Arbitration & Litigation as well as the further series of our comparative law articles. In particular:

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We hope you enjoy reading this issue! As always, we welcome your questions, suggestions and feedback. Please feel free to write to us anytime at **Arbitration.Germany@clydeco.com**

Yours
Clyde & Co Arbitration Team Germany

Germany more attractive as a place of arbitration? The German Federal Ministry of Justice plans a reform of the German Arbitration Law

On 18 April 2023, the German Federal Ministry of Justice announced its planned reform of the German Arbitration law in an effort to strengthen the attractiveness of Germany as place of arbitration.[1] The reform is to build upon the thorough revision of the German arbitration law by the adaption of the UNCITRAL model law[2] 25 years ago with the respective Act of 22 December 1997[3]. Since the coming into force of the German Arbitration law in 1998, a number of developments in the field of national as well as international commercial arbitration, like the revision of the UNCITRAL Model Law of 2006, the legal reforms in neighbouring to Germany countries (eg in France, Austria and Switzerland), the revisions of the arbitration rules of many major arbitral institutions, the advancing digitalization of procedural law, now dictate its further reform. The paper of the German Federal Ministry of Justice shall set the basis for a reform bill that – once adapted – would modify the 10th Book of the German Code of Civil Procedure, which regulates arbitration in Germany.

The German Federal Ministry of Justice identifies the following 12 key points that shall be the basis for drafting a bill to modernize German arbitration law:

- Arbitration agreements without form requirements in commercial transactions. This would allow formless, oral arbitration agreements in B2B transactions as already implemented in Option II of Article 7 of the UNCITRAL Model Law (2006). The high requirements of validity for B2C agreements shall remain unchanged.

- Introduction of provisions for the appointment of arbitrators in multi-party arbitration proceedings

- Possibility of judicial review (and annulment) of negative arbitral decisions on jurisdiction. Currently, only positive jurisdictional decisions are subject to such a review.

- Digitalisation of the arbitration proceedings. It should be possible to hold virtual hearings and also record them.

- Possibility to have the arbitral award published, subject to the parties' consent. The aim is to increase transparency in arbitration proceedings and to enable the further development of the law.

- In enforcement and setting aside proceedings as well as in judicial support proceedings, it shall be possible to submit both the arbitral award itself as well as other documents from the arbitration proceedings in English. This will speed up the proceedings and save the parties the costs of producing laborious translations.

- German Federal States that introduce Commercial Courts shall be able to declare these special panels of the Higher Regional Courts competent to decide on applications for the enforcement or the setting aside of arbitral awards. It shall be possible to conduct proceedings before the Commercial Courts entirely in English.

- In order to strengthen the integrity of arbitral proceedings, an additional remedy comparable to an action for restitution pursuant to Section 580 of the German Code of Civil Procedure shall be introduced. This remedy shall apply to final domestic arbitral awards where grounds for retrial of the case in litigation pursuant to Section 580 of the German Code of Civil Procedure are met.

1. https://www.bmj.de/SharedDocs/Gesetzgebungsverfahren/Dokumente/Eckpunkte_Schiedsverfahrensrecht.pdf?__blob=publicationFile&v=2
2. UNCITRAL Model Law on International Commercial Arbitration (1985).
3. Gesetz zur Neuregelung des Schiedsverfahrensrechts (Schiedsverfahrens-Neuregelungsgesetz - SchiedsVfG), 1 BGBl. I S. 3224.

– Measures of interim relief ordered by an Arbitral Tribunal shall be enforceable in Germany even if the place of arbitration is abroad.

– In the case of an application for a declaratory judgment on the admissibility or inadmissibility of arbitral proceedings pursuant to Section 1032 para 2 of the German Code of Civil Procedure, it shall also be possible to decide at the same time on the existence or validity of the arbitration agreement.

– Where appropriate, the court shall be able, at the request of a party, to refer a matter back to the arbitral tribunal after rejecting an application to declare the award enforceable and setting the same aside. Consequently, the annulment of the arbitral award shall, in case of doubt, result in the reviving the arbitration agreement with respect to the subject matter of the dispute.

– The power of the presiding judge of a state civil panel to make certain orders without prior hearing of the opposing party shall be limited to urgent cases.

In addition to the above, the German Federal Ministry of Justice wants to examine the following topics, in the course of drafting the bill:

– It shall be examined whether the German Code of Civil Procedure shall provide for a so-called emergency arbitrator, who can take interim measures before an arbitral tribunal is constituted. A further question is whether interim protection measures ordered in an arbitration with seat abroad should be enforced by the courts in Germany.

– It shall be examined whether a statutory provision on the admissibility of dissenting opinions should be integrated into the German Arbitration Law.

– It shall be examined whether there is a need on the part of the German Federal States to establish joint panels of judges from the Higher Regional Courts in arbitration cases across German Federal States borders.

– It shall be examined whether the taking of evidence or the performance of other judicial acts, for which the District Courts are currently responsible, shall be transferred to the Higher Regional Courts.

The German Arbitration Law as reformed with the previous Act of 22 December 1997 has rather stood the test of time, despite the developments in the domestic and international arbitration scenery. Nonetheless, the reform that the German Federal Ministry of Justice currently contemplates shall further modernize the Arbitration Law to meet the needs of arbitration practitioners for the years to come. This is an intention to be welcomed. However, since the paper published by the German Federal Ministry of Justice only set the basis for the bill that is yet to follow, it remains to be seen how and to what extent the legislator will take the above into account in the road to reform.

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Update on measures faced by foreign investors in Russia

Russia's invasion of Ukraine is still ongoing – and so are retaliatory measures by the Russian government that could potentially continue to impair foreign investments in Russia or contracts concluded with Russian entities. Following up on our earlier post in March 2022 outlining the initial set of measures (see Market Insight of 14 March 2022 **here**), it is time for an update.

As of January 2023, the course of the conflict remains unclear, so this update is intended to be a snapshot of some of the legal developments to date.

Potential nationalisation of foreign businesses and their assets

As previously reported, last February saw the first signs of concern that the Russian government might take actions to nationalise or expropriate foreign businesses and their assets. Decrees providing for such measures were enacted in short order at the beginning of 2022. Although there have not been reports of widespread expropriations, some prominent examples forewarn all foreign investors to stay vigilant and monitor the situation carefully.

The Russian government has established new operating companies for the Sakhalin-1 and Sakhalin-2 oil and liquified natural gas projects in the far east of the country, thereby essentially stripping foreign investors of their interests in the projects. A Presidential Decree allows foreign companies to apply to the government to have their shares transferred to the new operating company. Against this backdrop, two major western energy companies have decided not to apply for a transfer of their shares, resulting in a loss of the shares in the projects and billions of US dollars worth of investments.

One investor's previous attempt to sell its shares in the project was also blocked by Russia's retaliatory measures. The Russian President issued a Decree on 5 August 2022 that aims at banning transactions with certain assets in certain investment projects, absent a specific permission by the Russian government. Decree 520 is applicable to interests owned or controlled by persons from "unfriendly" countries (a list of countries published by the Russian government that are considered to commit unfriendly actions against Russia, Russian companies and citizens). It is currently only applicable to shares and interests in specific companies and projects, as well as companies and projects specifically from the energy and banking sectors.

This severely restricts an investor's ability to restructure or even exit their investments without permission from the Russian government. It is reported that this prevented one of the foreign energy companies invested in the Sakhalin-1 project from divesting its shares by selling them to another investor, before they were forcibly transferred to the new operating company.

The aircraft leasing sector was also one of the first sectors that was directly impacted by Russia's retaliatory measures. Several aircraft leasing companies incurred losses as they were unable to recover most, or all aircrafts leased to Russian airline companies. Disputes between leasing companies and their insurers on the potential insurance coverage of the "lost" aircrafts have since been reported. To date, it has been reported that foreign lessors have lost a total of 435 planes in Russia. In the meantime, it has also been reported that Russia plans to use over USD 22 billion until 2030 to replace the foreign made airplanes with domestic models.

Restriction related to the sale-purchase of interests in Russian limited liability companies

In March 2022, the Russian government imposed a special approval mechanism on purchase-sale of shares in Russian joint stock companies between residents and non-residents from "unfriendly" countries. This retaliatory measure adds further difficulties for foreign investors to divest from their business. This approval mechanism was extended on 8 September 2022 by Decree 618 to transactions relating to interests of Russian limited liability companies. The broad nature in which the Decree has been drafted, creates the possibility that the restrictions are not only limited to purchase-sale of stakes, but could extend to pledge or option agreements, management agreements or even shareholder agreements and articles of association, in case they would provide a targeted person or entity controlling or extensive rights. The Decree could also extend to indirect transactions occurring outside of Russia.

Potential restriction of patents and IP rights

The Russian government is continuing its discussions on potential restrictions of patent and IP rights. After already implementing a framework to essentially take over foreign patents without mandatory royalties, on 19 August 2022 a member of the Russian Duma introduced a bill that – if enacted – would enable courts to order compulsory licenses. The draft, essentially, addresses all rightsholders of copyrights, such as software, music, film etc., from "unfriendly" countries. The discussion on potential restrictions and IP rights in Russia is far from over and another space to continue to monitor closely.

Measures aimed at foreign currencies and the capital and financial markets

On 26 October 2022, Russia has taken measures with respect to financial services. This marks another escalation of the already far-reaching retaliatory measures by imposing an outright ban on dealings in or with shares or share capital of 45 banks and banking units, which are all either owned directly or through foreign capital by parties in countries that Russia considers "unfriendly".

The pre-existing prohibition to transfer or move any foreign currencies amounting to an equivalent of USD 10,000 outside the country has been extended until March 2023. Non-Russian natural or juridical persons that are from the so-called "unfriendly states" are further prohibited to transfer monies abroad from Russian bank accounts until March 2023.

Furthermore, Russian banks that are sanctioned by "unfriendly" countries may unilaterally convert any foreign currency deposits into Russian Roubles.

Investment Protection

There have been noteworthy developments with respect to investment protection in Russia. First, Russia has attempted to expand its territory by the purported annexation of four regions in eastern and south-eastern Ukraine: Luhansk, Donetsk, Kherson and Zaporizhzhia. Striking similarities with Russia's purported annexation of Crimea in 2014 can be drawn.

Given that arbitral tribunals as well as State courts have consistently found that Ukrainian investors could initiate investor-state arbitrations against Russia for damages caused to their investments by Russia in Crimea, the newly purported annexed regions could likely provide the same possibilities for investors that are damaged by Russia. Non-Russian investors in Luhansk, Donetsk, Kherson and Zaporizhzhia should review their investment structure and carefully keep track of all harm caused to their investment by Russia. Given that Russia has already hinted at taking control over private energy infrastructure, expropriations might follow suit. By purportedly annexing the Ukrainian regions, Russia has opened itself up to liability under its existing investment protection agreements.

Secondly, as previously reported, there is considerable dispute over the Energy Charter Treaty's (ECT) application in Russia for pre-2009 investments in Russia's energy sector, because the state never ratified the ECT. A recent court decision from August 2022 in Switzerland joins a 2021 decision from the Dutch Supreme Court to affirm the ECT's application. Russia, in its recent attempts, has failed to set-aside arbitral awards that are based on the ECT. It might be too early to identify an emerging pattern by arbitral tribunals and state courts that affirm the ECT's application with respect to investments made in Russia's energy sector before 2009. However, the current decisions are rather encouraging for investors and the potential protection of their investments under the ECT, conditional on whether (i) their investments are made in the energy sector and (ii) have been made pre-2009.

It has been reported that Ukraine and the EU are working towards establishing a War Claims Commission as a procedure to process reparation claims against Russia. International Claims Commissions have been successfully used in the past and can be designed for a specific situation. However, certain limitations exist that could make the claims commissions a difficult endeavour. First, Russia has not – and very likely will not – agree to the War Claims Commission. Establishing a commission with a treaty – without Russia's consent – is argued by some as a violation of the third-party rule of treaty law, namely that no state is bound by an agreement reached by others.

Second, Ukraine's plan to use frozen Russian assets in Western states for payment of the reparations is also considered legally difficult. Some argue that this would set a dangerous precedent and a violation of sovereign immunity, which is considered to also cover assets that states hold abroad. To this regard, several roadblocks still exist on the way to establishing a claims commission. The commission would be of unprecedented and unknown size, due to the fact that the war is still ongoing. If Ukraine succeeds and a Russia-Ukraine claims commission is to be established in the future, private claims for reparation from Russia for damages incurred because of the war will likely also be possible. Despite the overall concerns of using frozen assets for reparations, the Canadian government has started a first process to seize and pursue the forfeiture of a sanctioned Russian oligarch's assets to use the proceeds for the reconstruction of Ukraine and compensation of victims.

We also refer to our previous Insight of 14 March 2022 regarding the possibilities of such a claims commission and the more general enforcement difficulties (see Market Insight **here**).

Arbitrating Disputes with Russian Parties

Companies conducting business or with existing business in Russia or with Russian business partners might have arbitration agreements as robust dispute resolution clauses in their contractual agreements. Given the number of changes in the business environment and non-commercial considerations that have resulted from Russia's invasion of Ukraine, disputes could easily arise even for most prudent and diligent companies. In the current situation, even arbitral proceedings are not "business as usual".

Critically, in 2020, Russia passed legislation that provided for Russian courts' exclusive jurisdiction over disputes involving sanctioned Russian parties. The Supreme Court in a 9 December 2021 ruling upheld the law and decided that a sanctioned party could request an anti-arbitration injunction based on the legislation, regardless of whether the other party to the arbitration or the dispute has any connection to the country where the Russian party is sanctioned. Given the rising number of sanctioned companies and entities – as well as the nature of the sanctions – the risk that a dispute is connected to a sanctioned counterpart is more likely than ever. This could give Russian counterparties an excuse to not participate in an arbitration from the start.

Sanctions against Russian companies and state-owned entities are also feared to disrupt arbitral processes even if both parties are willing to proceed to arbitration. In summary, sanctions must be complied with by all natural and juridical persons within the territory of the state and all nationals of the state that enacted the sanctions, regardless of whether they are in- or outside of the state's territory. Different sanction regimes might have to be considered in a single arbitration depending on the nationality or residence of a party, arbitrator, counsel, witness or arbitral institution, the location of the seat of the arbitration or wthe place(s) the dispute is connected to. For example, an arbitrator or arbitral institution might be prohibited from receiving payment from a party, then Counsel may be prohibited from rendering legal services for a sanctioned party or an important but sanctioned witness might not be able to travel to an in-person-hearing.

On 15 March 2022, the EU had imposed sanctions that aimed at prohibiting transactions with Russian state-owned entities. The Arbitration Institute of the Stockholm Chamber of Commerce (SCC), Vienna International Arbitration Center (VIAC), Arbitration Institute of Finland Chamber of Commerce (FAI), Milan Chamber of Arbitration (CAM), German Arbitration Institute (DIS) and the Swiss Arbitration Centre reached out to the EU to address concerns by parties, counsel and arbitrators at their institutions regarding potential negative effects on access to and conduct of arbitral proceedings that involve Russian state-owned entities. This would not have only impacted arbitrations with state-owned entities as direct parties, but even the question as to whether an arbitral institution's bank could accept the transfer of funds from a party's bank that is a Russian state-owned entity. The EU reacted and on 21 July 2022 clarified that "transactions which are strictly necessary to ensure access to judicial, administrative or arbitral proceedings in a Member State, as well as for the recognition or enforcement of a judgment or an arbitration award rendered in a Member State" are not prohibited (Council Regulation (EU) 2022/1269 of 21 July 2022 amending Regulation (EU) No 833/2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine).

On 17 October 2022, the London Court of International Arbitration (LCIA) has likewise been granted a license from the UK's Office of Financial Sanctions Implementation for arbitrations administered and conducted under its own arbitration rules. The license allows the LCIA to process payments from parties for their costs of arbitration, even if they themselves or controlling entities are subject to UK's sanctions against Russia and Belarus in connection with Russia's invasion of Ukraine. The license also allows banks to process these payments.

While the EU and UK have clarified that sanctions should not hinder arbitral proceedings, some problems and issues remain. Secondary sanctions in force in other jurisdictions still cannot be ruled out entirely. Even with exceptions in place, banks for example might still be hesitant to process payments made to arbitral institutions by sanctioned entities. Or some sanctioned entities' banks might be disconnected from the SWIFT payment system and thereby not able to make payment. Additionally, it might be difficult for any Russian party or bank to make payment in the appropriate currency.

Overall, arbitrating disputes with respect to Russia and in particular sanctioned entities have become more complex. It requires careful considerations to ensure the effectiveness of an arbitral proceeding. Existing arbitration agreements are still used to settle dispute with Russian parties, as evidenced by the two German energy companies Uniper and RWE that reportedly brought two separate claims in December 2022 against Russia's Gazprom over missing gas deliveries. Given the war's impact on the gas and energy market, it is likely that this is only the tip of the iceberg of war-related arbitrations in the energy sector.

Enforcing arbitral awards

Sanctions may also impact enforcement of an award, because enforcement of an award under the New York Convention could be refused if a national court considers that the enforcement would be against public policy. While it is unlikely that sanctions are generally considered public policy, the existence of sanctions will give a resisting party an additional avenue of defence that could – and according to some in extreme cases – even be successful. It will also be practically difficult to enforce an award against a Russian party that had its assets outside of Russia frozen. Enforcement in Russia under the current circumstances might be considerably more difficult if not impossible at this time.

Enforcing arbitral awards against unwilling states, but particularly Russia, has a long and difficult history. Attempted enforcements have seen colourful examples of creative ways to enforce against unwilling states. The most recent example is an attempt to enforce an arbitral award by way of auctioning off seized trademarks of Russian vodka brands in the Netherlands. Russia ultimately lost its appeal against the attachment of the trademarks in November 2022, because the court found the vodka trademarks of commercial and not public purpose. In an unforeseen plot-twist the trademarks were not sold in an auction on 6 December 2022, because the received offers were considered to be too low. Given that we can expect more awards against Russia in the future, it will be crucial to build on past enforcement experiences and find creative ways to successfully enforce arbitral awards.

Furthermore, the Commercial Court of St. Peterburg and Leningrad in Russia decided on 30 December 2022 to freeze assets in the amount of nearly USD 500 million from a German company to prevent the company from disposing of its Russian assets. The petitioning Russian company successfully argued that it was intending to bring a HKIAC arbitration against the German company in excess of EUR 1 billion and because the imposed sanctions outside Russia would make subsequent recovery outside Russia impossible, the freeze was considered necessary to ensure the enforcement of the potential future award. This decision and its consequences highlight the complex situation all (potential) parties to a dispute face in the current situation with the plethora of sanctions and countersanctions that are in place.

If you have any questions on investment protection or arbitrating with Russian parties, please get in touch with **Georg Scherpf** (Clyde & Co, Hamburg).

For a detailed analysis of investment protection in the CIS region, please see the article published by Georg Scherpf (Clyde & Co) and Nikita Kondrashov (External) in the German Arbitration Journal (Investment Protection and Arbitration in the CIS Region **(SchiedsVZ 2020, 8 – beck-online)**. Georg Scherpf also co-authors the Article-by-Article Commentary of the ICSID Rules and Regulations 2022 (Editors Happ/Wilske, Beck, Hart, Nomos).

Georg Scherpf

Business protection: Tax Liability Insurance and Arbitration for effective risk management

Since Germany is not exactly known for its clear and easily applicable tax law, it is ultimately no surprise that a special form of hedging against known tax risks is becoming increasingly important, particularly in connection with M&A transactions. This is the so-called tax liability insurance, tax risk insurance or tax insurance. The following article sheds light on this newer insurance product and provides an overview of its main functions as well as potential coverage topics. It also discusses the role of arbitration in resolving disputes in this context.

Definition, scope and purpose of tax liability insurance

Tax Liability Insurance is a special type of insurance that insures a known but uncertain tax liability risk. The insurance compensates the policyholder for financial losses that may arise from tax liabilities or interest (including penalties or fines, if insurable) due to errors or irregularities in tax returns or tax audits, together with related litigation and legal defense costs (subject to an agreed deductible, if applicable). Companies are thus protected against the financial risks and costs that may arise in connection with tax matters. In this way, tax liability insurance also covers a gap in the insurance coverage of W&I insurance policies, which usually only cover unknown tax risks.

Tax liability insurance can be concluded in connection with an M&A transaction, but it can also take on independent significance, for example in the case of intra-group restructurings or prior to an IPO. In the case of an M&A transaction, the interested acquiring company will first carry out, among other things, a comprehensive tax due diligence. If any tax risks are identified or if there is a (slight) risk of such risks latently materializing - for example, because the interpretation of the relevant tax law with regard to the specific tax matter is not entirely clear and there is no case law from the highest courts, so that this assessment could be challenged by the tax authorities in the event of a future review - it may be worth taking out tax liability insurance. If any tax risks materialize, this can quickly lead to high additional claims by the tax authorities.

The tax risks covered are specifically defined in the respective policies and flanked by corresponding general or special coverage exclusions (for example, if the policyholder has intentionally or knowingly violated the law). All common types of taxes, for example value added tax, business tax, real estate transfer tax, etc., can be covered. Particular care should be taken when defining the insured tax risk, as in claims practice this is the linchpin of the coverage review. The insured event usually occurs according to the claims made (and reported) principle, whereby the respective policies contain special regulations as to when a loss must be specifically reported to the insurer.

Legal basis of tax liability insurance

Tax liability insurance is generally governed by the general provisions of insurance contract law. The relevant provisions of the German Insurance Contract Act (VVG) and the contractual agreements between the insurer and the policyholder apply. Whether the Tax Liability Insurance is functionally a liability insurance or a damage insurance in the sense of the VVG must be examined in each individual case. If the tax liability insurance, like a liability insurance, also covers the defense costs against a deviating tax assessment in addition to the indemnification with regard to the legally binding tax debt, there is much to be said for it being a liability insurance, so that the respective regulations in §§ 100 ff. VVG are also applicable. In this respect, it is therefore not surprising that the policies provide for comprehensive rights of the insurers to provide information or to cooperate.

Similar to W&I insurance policies, tax liability policies generally include certain warranties. These warranties may cover various aspects, such as the accuracy and completeness of the information and documents provided, compliance with all relevant tax laws and regulations, and disclosure of all relevant information to the tax authorities. In most cases, the parties will have linked risk exclusions to a breach of these given warranties. The legal consequences regime from Sections 19, 21 VVG must further be observed. The effects on the insurance cover of a breach of the guarantees therefore depend on the underlying insurance conditions. It is therefore important for the policyholder to carefully review all relevant information and documents and ensure that they comply with the guarantees set out in the policy. Insurers, on the other hand, should draft precise warranties and legal consequence provisions.

Disputes arising from tax liability policies before arbitration courts

Due to the complexity of German tax law and the large number of tax regulations that may be relevant to the interpretation of a tax liability policy in individual cases, disputes often arise between policyholders and insurance companies regarding the scope of coverage and the interpretation of the policy. In such cases, arbitration is often the way to go in order to resolve these disputes. This is because most tax liability policies (as well as W&I policies) contain arbitration clauses that prohibit the recourse to the ordinary courts.

Against this background, arbitration plays a significant role in resolving disputes relating to tax liability policies. Arbitration courts are independent and neutral decision bodies set up specifically to resolve disputes between parties. Compared to ordinary court proceedings, arbitration proceedings offer several advantages: They are usually faster, more confidential and more flexible. In addition, they allow the parties to choose experts with extensive knowledge of tax law as arbitrators, resulting in sound and specialized decisions.

Arbitration thus enables the parties to resolve their disputes in an efficient and focused manner. Arbitrators take into account the specific provisions of the policy, as well as relevant tax laws and regulations, to reach a fair decision. By choosing arbitration as a dispute resolution mechanism, parties can save time and money while ensuring that their disputes are handled by knowledgeable experts in the field of tax liability or insurance law.

Conclusion

Overall, tax liability insurance offers suitable protection against identified tax risks and can therefore be very helpful in corporate transactions or reorganizations. Whether tax liability insurance can offer sufficient coverage and protection in the event of a specific claim depends on various factors. Therefore, a thorough analysis of tax risks and exposures should be carried out in the underwriting process and the insured tax risks and warranties should be clearly described in the insurance terms and conditions. Should a claim ultimately arise, depending on the damage potential and complexity, it may also be helpful to involve legal advisors at an early stage in order to avoid arbitration proceedings if necessary or to ensure that they are handled competently and efficiently.

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The approach of the French courts to violations of international public policy: Cour de cassation pinpointing recent developments and trends

This is the first article in Clyde & Co's latest international arbitration series covering the scope of court powers on issues or violations of international public policy across various jurisdictions. In this piece, jurist Maria Mironova, from our Paris office, provides the legal perspective from France.

Under Article 1520, 5° of the French Code of Civil Procedure ("CCP"), an arbitral award shall be set aside if its recognition or enforcement is contrary to "international public policy"[1].

In 2017, in the ***Belokon*** case, the Paris Court of Appeal set aside a US$ 15 million arbitral award on the ground that the investor had been engaged in money laundering[2]. Subsequently, in the (long-awaited) judgment of 23 March 2022, the French Cour de cassation (Supreme Civil Court) confirmed the Court of Appeal's reasoning (the "Belokon judgment")[3], giving rise to much debate within the arbitration community. Although it had long been established that French courts' approach to annulment of arbitral awards under Article 1520, 5° of the CCP is particularly narrow, the *Belokon* judgment finally confirmed that this is no longer the case.

Intensity of the Court of Appeal's control: moving towards a broader standard.

"Minimalist" approach

Historically, French courts have taken a strong pro-enforcement stance on the issue, based on the well-established prohibition of review on the merits[4]. The so-called "minimalist" point of view was first taken by the Court of Appeal in the ***Thalès*** case in 2004[5] and confirmed by the *Cour de assation* in the **Cytec** case in 2008[6].

The applicable standard was based on the premise that a breach of international public policy had to be "*flagrant, actual and concrete*" for the award to be set aside, and that the Court of Appeal could not question the arbitral tribunal's findings, or accept new evidence for that matter.

That said, the "flagrancy" test meant that a breach had to be strikingly obvious and incontestable and, therefore, was often criticized as being overly cautious and even superficial.

1. "International public policy" under Article 1520, 5° of the CCP should be understood as an inherently French concept encompassing a set of rules and values that the French legal order may not disregard, even in international matters (Paris, 14 June 2001, Rev. arb., Vol. 2001, p. 773, note Ch. Seraglini).
2. Paris, 21 February 2017, ***Belokon v. Kirghizstan***, No. 15/01650, Rev. arb., Vol. 2017, p. 915, note M. Audit et S. Bollée. Note: while the most recent developments of French case law relate to allegations of corruption and money laundering, the same approach would presumably apply to other instances of international public policy violations.
3. Cass. Civ. 1st, 23 March 2022, ***Belokon v. Kirghizstan***, No. 17-17.981.
4. See, for example: Cass. Civ. 1st, 12 February 2014, No. 10-17.076 (also known as ***Schneider*** case): "Whereas the setting aside judge is the judge of the award in order to admit or refuse its integration into the French legal system, and not the judge of the case for which the parties have concluded an arbitration agreement; that having exactly retained that the action for setting aside was aimed, in reality, at a new investigation of the merits of the case, the Court of Appeal rightly rejected it".
5. Paris, 18 November 2004, ***Thales Air Défense v. Euromissile***, No. 02/19606, Rev. arb., Vol. 2005, p. 771.
6. Cass. Civ. 1st, 4 June 2008, ***SNF v. Cytec Industries BV***, No. 06-15.320, Rev. arb., Vol. 2008, p. 473, note I. Fadlallah; see also, on a corruption matter, Cass. Civ. 1st, 12 February 2014, No. 10-17.076.

Shift to the "maximalist" approach

The "minimalist" approach seems to have shifted in 2014, when the breach no longer had to be "*flagrant*"[7]. In 2016, the Court of Appeal added that the breach had to be "*manifest*", but ruled that it had the duty to "*seek, at law and in fact, all the elements allowing it to reach a decision on the alleged illegality of the contract*". While doing this, it was bound neither by the assessments made by the arbitral tribunal, nor by the substantive law chosen by the parties[8].

The Court of Appeal's reasoning in the ***Belokon*** case in 2017 is in fact just a continuation of this shift of view. Not only did the Court of Appeal apply the "maximalist" approach; it also asked whether there was "*serious, precise and converging*" evidence of money laundering operations – a low standard of proof that has been applied in matters of this kind ever since[9]. This new standard also reflects the "red flags" methodology of dealing with corruption (and, presumably, similar public policy allegations). This allows allegations to be proved by referring to a set of indirect indicia when it is difficult to do that by adducing direct evidence[10].

On 23 March 2022, the *Cour de cassation* eventually confirmed the "maximalist" approach, saying that the Court of Appeal had rightly held that the inquiry into the matter "*was neither limited to the evidence produced before the arbitral tribunal nor bound by [its] findings, assessments and qualifications*". The Cour de cassation also shifted from requiring the breach to be "*manifest, actual and concrete*" to requiring it to be merely "*in a characterised manner*" - a simpler and arguably more effective formula.

Court of Appeal's independent review extended to new evidence: nothing to worry about?

One concern that has been raised is that, by extending the scope of the Court of Appeal's review, the Belokon judgment might be crossing the line of reviewing an award on its merits.

However, the Cour de cassation explicitly pointed out that the Court of Appeal "*did not proceed with a new investigation or a revision of the merits of the award but made instead a separate assessment of the facts based solely on the consistency of the recognition or enforcement of the award with international public policy*".

In other words, according to the Cour de cassation, the Court of Appeal's role does not involve revisiting the tribunal's findings on liability or double-checking the relief granted. Its role remains within the ambit of Article 1520, 5° of the CCP and is limited to verifying whether the award's recognition and enforcement would hinder international public policy, and nothing more.

7. See, for example, Paris, 14 October 2014, ***Congo v. Commisimpex***, No. 13/03410, Rev. arb., Vol. 2014, p. 1030.
8. Paris, 27 September 2016, ***SA Ancienne Maison Marcel Bauche v. Indagro***, No. 15/12614.
9. See also: Paris, 16 January 2018, ***MK Group v. S.A.R.L. Oni***x, No. 15/21703, on obtaining a license for exploitation of natural resources by fraudulent means; and on contracts tainted by corruption: Paris, 28 May 2019, ***Alstom Transport v. ABL***, No. 16/11182, Rev. arb., Vol. 2019, p. 850, note E. Gaillard, quashed because the Court of Appeal distorted the evidence (Cass. Civ. 1st, 29 September 2021, No. 19-19.769); Paris, 17 November 2020, ***Sorelec v. Libya***, No.18/02568, Rev. arb., Vol. 2021, p. 762, note P. Mayer; Paris, 25 May 2021, ***Webcor v. Gabon***, n°18/18708, Rev. arb., Vol. 2021, p. 778, note P. Mayer.
10. See more on this in E. Gaillard, 'The emergence of transnational responses to corruption in international', in William W. Park (ed), Arbitration International, Oxford University Press 2019, Volume 35, Issue 1, pp. 1-19.

Another safeguard is that, in the *Belokon* judgment, the Cour de cassation has explicitly provided that, when the Court examines new evidence obtained outside of the arbitral proceedings, its duty is to "*ensure that the new evidence is being produced in conformity with the adversarial principle and equality of arms*". Indeed, it is only logical that the Court of Appeal could not possibly exercise its review by bypassing parties' right to have access to, examine and contest new evidence.

Court of Appeal's review of allegations raised for the first time: a promising trend?

The liberal approach adopted by French courts in the last few years can also be traced back easily to recent annulment judgments where the Court of Appeal examined corruption allegations despite the fact that they had not even been raised before the arbitral tribunal[11].

On 7 September 2022, in the ***Sorelec*** case, the Court of Appeal's approach was confirmed. The Cour de cassation held that the Court of Appeal had been correct in examining all the evidence in support of corruption allegations, "*regardless of the fact that such evidence had not previously been submitted before the arbitral tribunal*"[12].

On the one hand, admissibility of public policy allegations at the annulment stage might incentivise arbitral tribunals to inquire sua sponte (on its own initiative) into issues of corruption or other violations of international public policy, provided there are "red flags" giving grounds for suspicion.

There is already some arbitral case law in this vein[13], and the legal theory is favourable, holding that a sua sponte inquiry can be made (at least in corruption matters) if its subject matter is relevant to the outcome of the case and providing the tribunal does not violate the principle of due process[14]. Tribunals' proactive attitude could thus enhance enforceability of arbitral awards.

On the other hand, there is a tangible risk that public policy allegations are saved for the annulment stage, as part of a conscious procedural strategy. In the long run, this could undermine the attractiveness of arbitration and even jeopardize France's reputation as one of the most arbitration-friendly jurisdictions.

A recent development is that the Court of Appeal has already applied the Belokon standard of review in its latest decision of 5 April 2022 concerning a corruption matter, when it found that international public policy was violated "*in a characterised manner*" based on a sufficiently "*serious, precise and converging*" pattern of indicia, including those revealed after the arbitral proceedings concluded[15].

It remains to be seen how the "maximalist" approach will be applied going forward, and in particular whether a Pandora's box has been opened or not.

Maria Mironova

11. Paris, 17 November 2020, ***Sorelec v. Libya***, No.18/02568, Rev. arb., Vol. 2021, p. 762, note P. Mayer; Paris, 25 May 2021, ***Webcor v. Gabon***, No.18/18708, Rev. arb., Vol. 2021, p. 778, note P. Mayer; see also Paris, 13 April 2021, ***AD Trade v. Guinea***, No.18/09809; Paris, 5 October 2021, ***DNO Yemen v. Ministry of Oil and Minerals of Yemen***, No. 19/16601.
12. Cass. Civ. 1st, 7 September 2022, ***Sorelec v. Libya***, No. 20-22.118.
13. ***Metal-Tech Ltd. v. Republic of Uzbekistan***, ICSID Case No. ARB/10/3, Final award of 4 October 2013: "The Tribunal finds that it does not require the application of the rules on burden of proof or presumptions to resolve the present dispute. In this case, facts emerged in the course of the arbitration. Because those facts raised suspicions of corruption, the Tribunal required explanations"; ***Glencore International A.G. and C.I. Prodeco S.A. v. Republic of Colombia***, ICSID Case No. ARB/16/6, Final Award of 27 August 2019: "*The Tribunal agrees with Respondent that, provided that there are prima facie grounds for suspecting malfeasance, an international arbitration tribunal has the duty to investigate the facts, even sua sponte*"; ***ICC Award in Case 14470 of 2013***, in 'ICC Special Supplement 2013: Tackling Corruption in Arbitration': "*The Arbitral Tribunal cannot disregard the objection of invalidity due to illegality of the subject-matter, especially when such invalidity is due to corruption. This objection should be raised ex officio by the arbitrator*".

14. See, for example: E. Gaillard, 'La corruption saisie par les arbitres du commerce international', Rev. arb., Vol. 2017, pp. 805-838; D. Baizeau and T. Hayes, 'The Arbitral Tribunal's Duty and Power to Address Corruption Sua Sponte', in Andrea Menaker (ed), International Arbitration and the Rule of Law: Contribution and Conformity, ICCA Congress Series 2017, Volume 19, pp. 243-246.
15. Paris, 5 April 2022, ***Gabon v. Santullo Sericom***, No. 20/03242.

The approach of courts in England & Wales to violations of international public policy

This is the second article in Clyde & Co's latest international arbitration series covering the scope of court powers on issues or violations of international public policy across various jurisdictions. In this piece, associate Leonor d'Albiousse from our London office provides the legal perspective from England & Wales.

Under the New York Convention, the jurisdictions in which annulment of an international arbitral award may be sought are limited to the place where the award was made or under the law of which the award was made.[1] Consequently, an Award may face annulment in English courts when England was the seat of the arbitration or when the arbitration was conducted abroad but in accordance with English law.

The New York Convention set out limited grounds which can justify annulment of an arbitral award. Among these, Article V(2) provides that the court may refuse enforcement if it finds that the dispute was not arbitrable under the law of the state where the enforcement is sought or if the enforcement is contrary to the public policy of that state.[2]

Section 103(3) of the English Arbitration Act 1996 mirrors Article V(2) of the New York Convention, and sets out the limited grounds to challenge enforcement of an award, including, inter alia, when the award or the way in which it was produced is contrary to public policy.[3]

While other grounds may allow one party to challenge an award before English court, this article focuses on public policy violation as a ground to challenge arbitration awards, and how English courts interpret and apply public policy in this context.

1. New York Convention, Article V.
2. New York Convention, Article V(2).
3. Arbitration Act 1996, Article 68

Public Policy under English law

The New York Convention does not define the term "public policy", and it is therefore for each Member State to define freely and individually the scope of this ground for annulment. Public policy may include domestic public policy, i.e., the economic, legal, moral, political, and social values fundamental to one jurisdiction, and international public policy, i.e., fundamental principles pertaining to justice or morality that the State wishes to protect even when it is not directly concerned, and the duty of the State to respect its obligations towards other States or international organisations.[4]

Historically, public policy in English case law is understood quite narrowly and the threshold to annul an award on this ground is high. This reflects the pro-enforcement bias of the New York Convention, followed by England as an attractive and sophisticated seat for arbitration.

As far back as 1902, Lord Halsbury shrank the scope of public policy when he stated that public policy "does not leave at large to each tribunal to find that a particular contract is against public policy … you may say that it is because [certain things] are contrary to public policy they are unlawful, but it is because these things have been either enacted or assumed to be by the common law unlawful, and not because a judge or court have a right to declare that such and such things are in his or their view contrary to public policy".[5]

English courts are said to be reluctant to define public policy: "[c]onsiderations of public policy can never be exhaustively defined, but they should be approached with extreme caution … It has to be shown that there is some element of illegality or that the enforcement of the award would be clearly injurious to the public good or, possibly, that enforcement would be wholly offensive to the ordinary reasonable and fully informed member of the public on whose behalf the powers of the state are exercised".[6]

However, given the evolving nature of public policy, English judges seem to enjoy wide discretion to decide a case on the basis of public policy. In the words of Lord Baron Pollock CJ: "I think I am bound to look for the principles of former decisions, and not to shrink from applying them with firmness and caution to any new and extraordinary case that may arise".[7]

In the context of international arbitration, the parties to an illegal contract "cannot by procuring an arbitration conceal that they, or rather one of them, is seeking to enforce an illegal contract. Public policy will not allow it".[8] In *Soleimany v Soleimany*, the Court of Appeal refused, for reasons of public policy, to enforce an award of the Beth Din made in England that referred on its face to an illegal object of the underlying contract, namely to smuggle carpets out of Iran.

However, because a judge in an annulment proceeding does not review the actual merits of the award,[9] and annulment claims are usually heard by way of summary judgment, the threshold to annul an award said to violate public policy is relatively high.

4. International Law Association Recommendations on the Application of Public Policy as a Ground for Refusing Recognition or Enforcement of International Arbitral Awards, Annex to Resolution 2/2002 on International Commercial Arbitration, adopted at the 70th Conference of the International Law Association held in New Delhi, India, 2-6 April 2002. See also, IBA Report on the Public Policy Exception in the NY Convention, October 2015.
5. Janson v Driefontein Consolidated Mines [1902] AC 484.
6. Deutsche Schachtbau- and Tiefbohrgesellschaft mbH v. Ras Al Khaimah National Oil Co., Shell Intl Petroleum Co. Ltd., Court of Appeal, 24 March 1987. See also, IBA Report on the Public Policy Exception in the NY Convention, October 2015, p.9.
7. Egerton v Brownlow 10 E.R. 359, (1853) 4 HL Cas 1 at 149.
8. Soleimany v Soleimany [1999] QB 785 at 800.
9. Section 81(2) of the Arbitration Act 1996 states: 'Nothing in this Act shall be construed as reviving any jurisdiction of the court to set aside or remit an award on the ground of errors of fact or law on the face of the award.'

In *Profilati v Paine Webber*, Moore-Bick J stated that "*where the successful party is said to have procured the Award in a hich is contrary to public policy, it will normally be necessary to satisfy the Court that some form of reprehensible or unconscionable conduct on his part has contributed in a substantial way to obtaining an Award in his favour. Moreover I do not think that the Court should be quick to interfere under this section*".[10]

Similarly in *Honeywell International Middle East Limited v Meydan Group LLC* allegations of bribery during a tender process did not allow the defendant to resist the enforcement in England of a Dubai arbitration award relating to payment default under an electrical works contract. In this case, the defendant argued that the award should be set aside because the underlying contract in the arbitration had been procured illegally, after the Claimant had bribed public servants in Dubai. In deciding the case, Ramsay J observed that bribery had not been established and that, even if Meydan's case on bribery succeeded, contracts procured by bribes were not unenforceable in England, but rather were voidable at the innocent party's election, with counter-restitution. The court confirmed that the threshold to set aside an award on the basis of public policy violations is very high when it held that "public policy should only be invoked in clear cases".[11]

While judges enjoy wide discretion to decide these cases, they are not meant to review the merits and therefore the threshold required to establish a violation of public policy is high. On the other hand, public policy is continuously evolving and judges are not bound by many precedents, which gives counsel the opportunity to be creative when building their arguments on this ground.

Leonor d'Albiousse

10. Profilati v Paine Webber [2001] 1LLR 715, at page 719–780.
11. Honeywell International Middle East Ltd v Meydan Group LLC [2014] EWHC 1344 (TCC) at para. 93.

The annulment of arbitral awards for violation of international public policy under Spanish law

This is the third article in Clyde & Co's latest international arbitration series covering the scope of court powers on issues or violations of international public policy across various jurisdictions. In this piece, associate Sofía Rivas and trainee Michelle Donovan from our Madrid office provides the legal perspective from Spain.

Introduction

Arbitration is one of the best known and most widely used alternative dispute resolution (ADR) mechanisms at an international level. This mechanism consists of entrusting the final settlement of a dispute to a third party, which may be an arbitrator or an arbitral institution.

It is well known that one of the most relevant characteristics of international arbitration is the importance given to the principle of "party autonomy". Even so, arbitration is not free from limitations. Specifically, one of the grounds for annulment of an arbitration award is that it is contrary to "public policy". Under Spanish law, this limitation is set forth in Article 41 f. of Law 60/2003, dated December 23, 2003, on Arbitration.

In particular, if one of the parties considers that the award is contrary to public policy, they may file an "action for annulment". This initiates a process of external judicial control over the validity of the award which, in Spain, falls within the jurisdiction of the High Courts of Justice.

In this article, we will analyse the limitation of public policy in international arbitration, with a special reference to Spanish jurisdiction. In this way, we aim to clarify and provide a concrete perspective on this complex concept.

Public policy concepts in international arbitration. Special mention to Spanish jurisdiction.

First of all, one should recognise that public policy is an extremely "open" and "indeterminate" term. For its interpretation, not only international norms come into play, but also the internal regulations of each State.

Nevertheless, many arbitral tribunals have tried to frame this concept by defining it as "an international consensus as to universal standards and accepted norms of conduct that must be applied in all fora" or as "*a series of fundamental principles that constitute the very essence of the State, with the essential function [...] to preserve the values of the international legal system against actions contrary to it*".

In other words, public policy reflects the global consensus on international economic, legal, moral, political and social values. Among these, corruption stands out as one of the main areas of concern and development.

Regarding Spanish jurisdiction, this concept has traditionally been interpreted in a very restrictive manner. More precisely, it has been defined as the core of fundamental rules or principles that govern the organisation and functioning of society. In this sense, we mention the Judgment of the Provincial Court of Madrid dated May 26, 2000, which ruled as follows:

> *"Material public policy is understood to be the set of public, private, political, moral and economic legal principles which are absolutely mandatory for the preservation of society in a given nation and at a given time (...) and from a procedural point of view, public policy is configured as the set of necessary formalities and principles of our procedural legal system, so that an arbitration that contradicts any or some of such principles may be declared as null for the violation of public policy".*

Therefore, we can understand that public policy acts as a necessary and indispensable limit to the principle of party autonomy, in order to guarantee the effectiveness of the constitutional rights of citizens and the functioning of institutions. This definition can be completed by saying that it also ensures "the protection of the concepts and values inspiring the constitutionally enshrined system of social democracy". In addition, public policy acts as a "limit that is also imposed on the arbitrator and which the latter may not go beyond, this ground for nullity constituting a jurisdictional control of that limit in order to ensure that arbitration decisions respect that set of indispensable values and rights". (Judgment of the Provincial Court of Valencia, dated February 6, 2002).

The action for annulment of arbitral awards under Spanish Jurisdiction

As a member of the European Union, Spain is subject to EU law, and therefore to the rulings of the CJEU. This court has also ruled on what should be understood by "public policy".

In particular, the CJEU has adopted a firm position on the matters which it is considered to be "fundamental" and "essential" to preserve. Specifically, it has ruled that arbitration awards may be annulled for lack of public policy when their content (i) is contrary to competition law; or (ii) contravenes the rules on unfair terms in consumer contracts (Directive 93/13/EEC).

In Spain, it is settled law that an arbitration award cannot be reviewed on the merits and that it is not the national courts' task to correct the arbitrators' hypothetical errors.

Specifically, the Judgment of the High Court of Justice of the Basque Country dated April 19, 2012, stipulated that the cause of annulment of arbitral awards by judges must have "*a reduced role that limits its operability, in congruence with its nature, to truly exceptional cases" and this "is only possible on the basis of a limited conception of public policy*".

Along these lines, the Judgments of the High Court of Justice of Madrid dated May 21, 2013, and April 21, 2015, as well as the Judgment of the High Court of Justice of Murcia of March 10, 2014, have recognised that "*the concept of public policy cannot become a trap door to allow the control of the substantive decision adopted by the arbitrators*".

More recently, the Judgments of the High Court of Justice of the Canary Islands of March 10, 2021, and of Castilla-La Mancha of March 22, 2021, have stated that the safeguarding of public policy cannot "*imply that the judges hearing the annulment of the arbitral award replace the criterion reached by the arbitrator. In addition to the fact that the notion of public policy cannot be taken as a power of veto (…) that allows the control of the arbitral decision*".

As can be seen, Spanish case law has sought to limit the control of judges over arbitral awards, limiting their work to tasks of support, assistance and external control (Supreme Court Judgment of June 22, 2009).

Recent Spanish case law

To explore this matter further, it is worth referring to the most recent Spanish judgment on this issue, namely Constitutional Court Ruling No. 17/2021 of March 22, 2021, (EDJ 2021/510947), which analyses a decision of the Supreme Court (SC) that annulled an arbitration award. According to the SC decision, the award did not comply with the right to effective judicial protection (Article 24 of the Spanish Constitution) and was therefore contrary to public policy. The SC based its decision on the following grounds:

- Failure to state reasons.
- Failure to assess evidence.
- Failure to rule on all the issues raised in the arbitration.

The SC's decision was appealed before the Spanish Constitutional Court, which found that the ruling had erred in deciding to annul the award, as it did not violate public policy. In particular:

- Arbitral awards should be considered final decisions, and therefore judicial review of awards should be kept to a minimum.
- For the award to be declared null and void, it must be "arbitrary, illogical, absurd or irrational".
- The role of the court at the annulment stage is not to replace the arbitrator in the resolution of the dispute, as no new analysis can be made of issues that have already been decided.
- The fundamental role of the tribunal is to verify that the arbitrators have respected due process and procedural guarantees.

Conclusion

As can be seen, the concept of public policy is still subject to interpretation, as there is still no settled or unanimous definition of it. However, the Spanish courts have shown an increasingly "pro-arbitration" trend, especially following the recent Constitutional Court's ruling of March 22, 2021. In this way, Spain is positioning itself as a country in favour of treating arbitral awards as final decisions, limiting the actions of judges to external control, and therefore guaranteeing minimal intervention.

Sofía Rivas

Michelle Donovan

Public policy challenges to arbitration awards in the United Arab Emirates

This is the fourth article in Clyde & Co's latest international arbitration series covering the scope of court powers on issues or violations of international public policy across various jurisdictions. In this piece, associate Moamen Elwan from our Dubai office provides the legal perspective from the UAE.

The United Arab Emirates (**UAE**) is unique in that it is a country with two legal systems and three sets of arbitration laws. Public policy remains a vexed issue and the lack of any coherent principles, particularly in the onshore regime, has led to uncertainty.

Overview of the onshore arbitration law

The UAE ratified the New York Convention in 2006. A 'new' arbitration law based largely on the UNCITRAL Model Arbitration Law was issued in 2018 (the **UAE Arbitration Law**). Consistent with other jurisdictions, public policy is one of the grounds that may be invoked as a basis for challenging the enforcement of a foreign arbitration award or annulling (in whole or in part) a domestic arbitration award.[1]

Overview of the offshore arbitration laws

Within the UAE there are two common law based 'offshore' jurisdictions: (1) the Abu Dhabi Global Market (**ADGM**) and (2) the Dubai International Financial Centre (**DIFC**). These jurisdictions have their own legal and regulatory frameworks in relation to civil and commercial matters which are modelled on the English/common law system. The DIFC and ADGM also have their own arbitration laws: DIFC Law No. 1 of 2008 and ADGM Arbitration Regulations 2015. These laws are based on the UNCITRAL Model Law and contain similar public policy exceptions in relation to the enforcement/annulment of arbitration awards, in turn based on the "*public policy of the UAE*".

1. Article 53 of the UAE Arbitration Law.

Public policy onshore

The UAE Arbitration Law does not draw a distinction between international and domestic public policy. It simply provides that an arbitration award should not conflict with the "*public order and morality of the State*." There is no exhaustive list to determine whether something is an issue of public policy/order/morality and the matter is in a state of flux; so what might be considered a rule of public policy in the past might not be regarded as such in the future and vice versa.

Article 3 of the UAE Civil Code provides guidance on the sorts of matters that may be considered issues of public policy. However, the definition is extremely broad and includes issues relating to:

[…] personal status such as marriage, inheritance, and lineage and matters relating to systems of government, freedom of trade, the circulation of wealth, rules of individual ownership and the other rules and foundations upon which society is based, in such a manner as not to conflict with the definitive provisions and fundamental principles of the Islamic sharia.

Case law has identified several other markers of public policy including:

– bankruptcy/insolvency;[2]

– interest rates (above those stipulated by law);[3] and

– land/title registration.[4]

In an important development in the commercial context, the Dubai Court of Cassation found that disputes arising out of agency contracts could be subject to arbitration. The case arose out of an agency contract subject to arbitration in the Netherlands under the rules of the Netherlands Arbitration Institute. In its decision in Dubai Court of Cassation, Challenge No. 993 of 2017, the court considered Article 226 of the (now repealed) Commercial Code of 1993, requiring that the court in which circuit the agency agreement was executed has jurisdiction over the dispute arising out of that agency agreement. The court determined that Article 226 applies only when the state courts have jurisdiction but does not apply when the parties to the agency agreement agree to arbitrate. In its reasoning, the court differentiated between the functional and territorial jurisdiction of the courts and considered that Article 226 deals with the territorial jurisdiction while the issue related to the functional jurisdiction of the arbitral tribunal, which is not relevant for the purpose of Article 226. This is a welcome approach because Article 6 of the Commercial Agencies Law was historically regarded to grant the local courts exclusive jurisdiction over all disputes arising out of commercial agencies as a matter of public policy.

2. Supreme Federal Court, Challenge No. 493 of JY18, dated 26 October 1997.
3. Dubai Court of Cassation, Challenge No. 146 of JY 2008.
4. Dubai Court of Cassation, Challenge No. 320 of JY 2014.

Public policy offshore

Given the relative infancy of the offshore regimes, particularly the ADGM, there is limited guidance on public policy.

In *Loralia Group LLC v Landen Saudi Company* [2018] the DIFC Court confirmed that the public policy of the DIFC is the same as that of the wider UAE, whilst acknowledging that the outcomes may differ:

I need not be convinced that the public policy referred to in Article 41 of the DIFC Arbitration Law refers to the same public policy of the UAE as a whole. This is an uncontroversial finding at this time […] While the outcomes may differ, the public policy applied is actually the same. Public policy of the UAE encompasses the constitutional and legislative creation of the DIFC and thus incorporates the intended differences legally allowed within the DIFC.[5]

In *Lucinethlucineth v Lutinalutina Telecom Group Ltd [2019]*[6], the court set out guidelines on when a public policy type argument may be invoked:

– where the award fundamentally offends the most basic and explicit principles of justice and fairness; and

– where the award is contrary to the essential morality of the state in question or discloses errors that affect the basic principles of public and economic life.

Conclusion

The UAE has two legal systems and three sets of arbitration laws. Although the systems may differ, the reference appears to be to the same notion of public policy; albeit, with potentially different outcomes. The definition of public policy adopted in the UAE Civil Code is extremely broad and encompasses matters such as the "*freedom of trade*", "*circulation of wealth*" and "*rules and foundations upon which society is based*". This has led to a lack of consensus and it remains the case that there is, understandably, an evolving definition of the notion of public policy.

Nils de Wolff

Moamen Elwan

5. Judgment of H.E. Justice Shamlan Al Sawalehi, Loralia Group LLC v Landen Saudi Company [2018] DIFC ARB 004 dated 20 June 2019.
6. Order with reasons of H.E. Justice Sir Jeremy Cooke, Lucinethlucineth v Lutinalutina Telecom Group Ltd [2019] DIFC ARB 005, dated 8 August 2019.

Full, Partial or Plausibility Review? – Public Policy and the Level of Scrutiny Applied by German Courts

This is the last article in Clyde & Co's international arbitration series covering the scope of court powers on issues or violations of international public policy across various jurisdictions. In this piece, Counsel Georg Scherpf, Associate Antonios Politis, and Research Assistant Benedikt Kaneko from our Hamburg office provide the legal perspective from Germany and highlight a recent judgment, in which the German Federal Court of Justice clarified the level of scrutiny German state courts apply in cases of potential violations of public policy and in case of a violation of antitrust laws (Bundesgerichtshof, decision of 27 September 2022 – KZB 75/21).

A recognized advantage of arbitration is the possibility to enforce arbitral awards in almost any jurisdiction. This nearly universal enforcement is based on the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, which is currently signed by 171 parties, including Germany. Under the Convention, the grounds for refusal to enforce and recognize an arbitral award are **very limited**. Domestic courts can refuse the enforcement and recognition of an arbitral award inter alia under Article V(2)(b) New York Convention, if the recognition or enforcement would be contrary to public policy of that country. The UNCITRAL Model Law, on which Germany's arbitration law is primarily based, has incorporated Article V(2)(b) of the New York Convention in its Articles 34(2)(b)(ii), 36(1)(b)(ii).

Germany has adopted these provisions in its arbitration law, which provides domestic courts with the authority to set aside arbitral awards stemming from arbitrations seated in Germany and refuse the recognition and enforcement of domestic and foreign arbitral awards, if – among some limited other grounds – the recognition or enforcement of the arbitral award would lead to a result that is contrary to public policy (Sections 1059 (2) No. 2b, 1060 (2) German Code of Civil Procedure – *Zivilprozessordnung* for domestic awards and Section 1061 German Code of Civil Procedure referring to Article V(2)(b) of the New York Convention for foreign awards). Given that neither the Convention nor the Model Law further define the term, it is left to the State courts to interpret its meaning, which opens it up to diverging interpretations across jurisdictions.

This short article focuses on how German courts understand, interpret and apply the concept of public policy in arbitration-related proceedings and, in particular, what level of scrutiny a German court may apply when examining an arbitral award: If a violation of public policy is suspected, would a German court have to reopen the entire case and possibly even proceed to the taking of evidence stage, or is the review just necessary for "obvious" or manifest violations of public policy? Generally, German courts were strictly limited to reviewing obvious and manifest violations, although there was some debate among several German Higher Regional Courts (*Oberlandesgerichte*) in the context of antitrust law to broaden the review. A recent and much discussed decision by the German Federal Court of Justice (*Bundesgerichtshof* – BGH) has for now ended this judicial debate (BGH, decision of 27 September 2022 – KZB 75/21).

The Interpretation of Public Policy in German Arbitration Law

According to the established definition recently confirmed by the BGH (Decision of 16 December 2021 – I ZB 31/21), a violation of public policy occurs if the arbitral award (or its declaration of enforceability) is manifestly incompatible with essential principles of German law, i.e. if it "*violates a norm that regulates the foundations of state or economic life, or if it is in intolerable conflict with German perceptions of justice*". Naturally, a violation of mere dispositive law is not included, as deviation from such is a matter of party autonomy. However, not all violations of mandatory law constitute a violation of German public policy either. Rather, the norm in conflict must be an expression of a value decision by the legislator that is fundamental to the legal system. This, however, will only apply in the most exceptional cases (see BGH, decision of 28 January 2014 – III ZR 40/13 and decision of 8 May 2014 – III ZR 371/12).

In terms of examples, such "exceptional" cases are usually divided into substantive and procedural violations of German public policy:

- Substantive violations cover cases in which the contents of the arbitral award are incompatible with the fundamental concepts of the German legal system (see, Higher Regional Court of Munich, decision of 30 July 2012 – 34 Sch 18/10 and Higher Regional Court of Saarbrucken, decision of 30 May 2011 – 4 Sch 03/10). Such a violation has been found if the arbitral tribunal orders a party to undertake an illegal action (see, Higher Regional Court of Munich, decision of 30 July 2012 – 34 Sch 18/10) or to a conduct that would violate antitrust law (see, Higher Regional Court of Dusseldorf, decision of 21 July 2004 – Sch(Kart)1/02). Furthermore, a substantive violation of German public policy is thinkable where a party is ordered to pay gambling debts or punitive damages.

- Procedural violations of public policy have been found if the decision was rendered on the basis of a procedure that deviates from the fundamental principles of German procedural law to such an extent that it cannot be regarded as having been rendered in an orderly procedure governed by the rule of law (see, BGH, decision of 15 May 1986 – III ZR 192/84), even when taking into account that an arbitral proceeding potentially differs significantly from State court proceedings. Procedural violations are often violations of the principle of the right to be heard (Article 103 (1) German Constitution – *Grundgesetz*), which is also considered a cornerstone of arbitral proceedings. Other fundamental principles of a procedure that, if not met, can lead to a violation of public policy include the independence and impartiality of the arbitrators, the equality of the parties and the right to a fair trial.

Importantly, the above-mentioned standards for procedural law also apply to foreign-seated arbitrations and resulting awards to be enforced in Germany. In this context, however, the BGH distinguishes between an *ordre public interne* applicable in proceedings concerning domestic awards and an *ordre public international* for foreign awards. In the interest of international trade, it is well-established court practice in Germany to apply the latter standard when considering whether the enforcement of a foreign award would be against public policy (see, e.g., BGH, decision of 2 March 2017 – I ZB 42/16 and decision of 6 October 2016 – I ZB 13/15). One should not be confused by this distinction: the *ordre public international* in this context still refers to a public policy assessment from the vantage point of German law. At most, the *ordre public international* is considered to be a slightly less stringent standard of review than the *ordre public interne* (BGH, decision of 2 March 2017 – I ZB 42/16, para. 21). In any case, this will only lead to marginally different results under the two standards, if at all.

Level of Review and Scrutiny by German Courts

The most important practical consideration when applying the above definition is what level of scrutiny State courts may apply when examining an award for possible violations of public policy. Internationally, this question is answered in very different ways (*see, e.g.*, the newest developments in France). In Germany, the general rule is that courts will not review the merits of an arbitral award and, in particular, will not conduct a *de-novo* review of the merits. This so-called prohibition of a *révision au fond* prohibits courts from replacing an arbitral tribunal's assessment of the evidence with its own assessment. To prevent a review through the backdoor for factual correctness of the award by way of an extensive scrutiny and review for a public policy violation, the BGH generally requires the violation of *ordre public* to be obvious or manifest (see, BGH, decision of 28 January 2014 – III ZB 40/13). This was understood to generally limit a court's level of scrutiny.

However, there was some debate between several Higher Regional Courts on whether this general prohibition of a révision au fond must have a universal application or whether, in relation to particularly significant areas of law, a more in-depth examination should be possible. The debate specifically concerned the area of antitrust law as a result of the public interest in a proper functioning competition. Here, the views ranged from a very far-reaching review of the arbitral award for violations of antitrust law, including not only the legal findings but also the judicial determination of the facts (*see, e.g.,* Higher Regional Court of Celle, decision of 14 October 2016 – 13 Sch 1/15 Ls. 2, at para. 89, and Higher Regional Court of Düsseldorf, decision of 21 July 2014 – VI-Sch (Kart) 1/02, Sch (Kart) 1/02, paras. 24 et seq.), to a review of only the grossest and most obvious violations of public policy (*see, e.g.,* Higher Regional Court of Thuringia, decision of 8 August 2007 – 4 Sch 03/06). Most recently, the Higher Regional Court of Frankfurt held that only a very limited review of an arbitral tribunal's application of antitrust law was to take place, since a separate antitrust review competence of the State court would be incompatible with the nature of arbitration as a private form of dispute resolution, because the decision of the parties to transfer the power to decide disputes to a tribunal would be undermined (Higher Regional Court of Frankfurt, decision of 22 April 2021 –26 Sch 12/20, para. 79).

In its recent ruling from 27 September 2022 (KZB 75/21), the BGH overturned the Higher Regional Court of Frankfurt's ruling on the scope of review and thereby put an end to this debate. The BGH held that, at least for certain "core" antitrust law provisions (such as Sections 19, 20, and 21 German Competition Act – "Gesetz gegen Wettbewerbsbeschränkungen", including prohibitions with respect to the abuse of market power positions and other restrictive behavior) that form part of Germany's ordre public, the courts are not limited in their review and may scrutinize an arbitral award for a violation of these provisions in fact and in law.

Recognition and enforcement of an arbitral award that incorrectly applies elementary foundations of the legal order and the fundamental norms of antitrust law would lead to a result that would be "obviously" incompatible with essential principles of German law. No legal system could accept that violations of its most fundamental standards are confirmed by its own courts, regardless of whether or not these violations are manifest or obvious (see, para. 15 of the BGH's recent ruling). Therefore, insofar as the application of such elementary rules of the legal system is at issue, the prohibition of révision au fond does not apply, leading to a full review of the award in fact and law ("uneingeschränkte Kontrolle in tatsächlicher und rechtlicher Hinsicht"). In the BGH's view, this is particularly true for antitrust law, because the rules in question would not only serve the interest of the parties to the arbitration, but the preservation of the public interest in a functioning competition (para. 16). Because an obvious (in the sense of "readily detectable") violation of antitrust law may only be considered in rare circumstances, courts would often be precluded from conducting an appropriate review taking into account the complexity of antitrust cases (para. 17). Without a full review, this public interest would not be adequately protected.

As a result, as far as the question of a violation of core provisions of antitrust law (such as the prohibition of cartels or abusive practices) is concerned, the state judge may therefore not simply resort to a mere review of plausibility or of readily detectable violations but must conduct a full review in fact and law. Ultimately, one could even argue that this decision institutes a de facto right to appeal arbitral awards if and to the extent they concern the application of antitrust law.

Conclusion and Outlook

Certainly, the BGH's decision will have significant consequences for arbitral awards in cases with antitrust implications. However, this limitation of the prohibited révision au fond should be seen as confined to the core provisions of antitrust law. Overall, for most potential public policy violations – and in particular all of those that only concern the parties to the dispute (e.g., potential procedural public policy violations) – the scope of German courts' review will continue to be narrowly limited.

It remains to be seen to what extent this limited suspension will result in a new trend and whether possible violations of other areas of law will soon be subject to full review by German courts, too. Looking ahead, the question will be which norms are to be seen as elementary, the violation of which would automatically be accompanied by an "obvious" incompatibility with the German legal system. However, since the BGH is generally regarded as "arbitration-friendly" and will not want to diminish the special advantages of arbitration proceedings (e.g., finality of arbitral decisions), it is likely that the BGH will tread carefully here.

This Case Comment has first been published on the **JusMundi-Blog** and was later reprinted.

Georg Scherpf

Antonios Politis, LL.M. (NYU)

Green light for enforcement of investor-state arbitration award in Australia

The High Court of Australia has delivered its highly anticipated decision in Kingdom of Spain v Infrastructure Services Luxembourg Sàrl [2023] HCA 11. The decision recognised and enforced an ICSID arbitration award obtained by a renewable energy investor against the Spanish Government for €101 million.

The case is significant, as it is a rare Australian example of a contested application for recognition and enforcement of an investment treaty award and contains useful guidance on the interpretation of the ICSID Convention and the extent of foreign state immunity. The case is also topical given current debates about the legitimacy and transparency of investor-state dispute settlement and its increasing use as a forum for climate-related claims.

Background to the dispute

The dispute is one of many arising from the withdrawal of renewable energy subsidies offered by the Spanish Government in the early 2000s. Following the global financial crisis and a change of government, Spain started to withdraw these subsidies from 2013. This has led to more than 50 cases issued against Spain by foreign investors in renewable energy projects alleging breaches of the multilateral Energy Charter Treaty (1994) (**ECT**). The ECT allows investors to bring direct claims against contravening states and contains an arbitration agreement providing for settlement of disputes under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965) (**ICSID Convention**).

The present dispute involves investors from Luxembourg and the Netherlands who initiated an ICSID arbitration against Spain for alleged breaches of the ECT. In 2018, the investors obtained an ICSID award against Spain for €101 million (along with interest and part of their legal costs).

The award remains unpaid by the Spanish Government. The investors sued in the Federal Court of Australia seeking enforcement of the ICSID award against Spain.

As a result of developments in European Union case law and regulation, enforcement of awards arising from intra-EU disputes under the ECT and other treaties has become more difficult (or impossible) in EU jurisdictions. Hence investors are looking to non-EU jurisdictions, such as Australia, as venues for enforcement.

ICSID Convention

The primary purpose of the ICSID Convention is to promote the flow of private capital to sovereign nations by mitigating sovereign risk. The ICSID Convention is intended to provide certainty to private investors by facilitating the resolution of disputes in cases where a State defaults on its obligations undertaken towards investors in relevant bilateral or multilateral investment treaties.

The ICSID Convention has been given the force of law in Australia under the International Arbitration Act 1974 (Cth), s 32. Relevantly to this case:

- **Article 53** provides that an ICSID Convention award shall be binding on the parties.
- **Article 54** provides that each Contracting State shall recognise an ICSID award as binding and enforce the pecuniary obligations imposed by that award "as if it were a final judgment of a court in that State".
- **Article 55** preserves state immunity from "execution" of an award.

Enforcement in the Australian courts

In 2019, the investors brought proceedings to enforce the ICSID award obtained against Spain in the Federal Court of Australia, pursuant to Article 54 of the ICSID Convention.[1]

Spain resisted enforcement, asserting that as a foreign state it was immune from recognition and enforcement proceedings under the *Foreign States Immunities Act* 1985 (Cth). Section 9 of that Act provides that foreign states are immune from the jurisdiction of the Australian courts, except as provided for in that Act. One such exception is where the foreign state has submitted to the jurisdiction of the Australian courts, including by way of a treaty (*Foreign States Immunities Act*, ss 3, 10).

At first instance, Stewart J granted the investors' application for enforcement, rejecting Spain's plea of foreign state immunity with respect to recognition and enforcement of the award (but not execution) and ordering Spain to pay €110 million to the investors.[2] On appeal, the Full Federal Court (Allsop CJ, Perram and Moshinsky JJ) also concluded that Spain had waived its foreign state immunity in relation to the recognition of the ICSID award in Australia and perhaps enforcement (but, again, not execution).[3] The Full Court ordered that the award was binding on Spain and entered judgment against Spain for €101 million.[4] However, the Court noted that any immunities of Spain against execution of that judgment were unaffected.[5]

Spain brought a further appeal from the Full Federal Court to the High Court of Australia. In a unanimous decision of all 7 justices, the High Court dismissed Spain's appeal, as set out in further detail below.

1. The Federal Court of Australia is designated as a competent court for this purpose by the *International Arbitration Act*, s 35(3).
2. Eiser Infrastructure Ltd v Kingdom of Spain (2020) 142 ACSR 616; [2020] FCA 157
3. Kingdom of Spain v Infrastructure Services Luxembourg Sàrl (2021) 284 FCR 319; [2021] FCAFC 3
4. Kingdom of Spain v Infrastructure Services Luxembourg Sàrl (No 3) (2021) 392 ALR 443; [2021] FCAFC 112
5. See [2021] FCAFC 3 at [6]

The High Court's decision

The key issue in the appeal to the High Court of Australia was whether Spain could plead foreign state immunity as a defence to the recognition and enforcement of the ICSID award by the Australian courts. The Court held (in a single, joint judgment) that Spain's agreement to the ICSID Convention amounted to a waiver of its immunity from recognition and enforcement of the award.

The key points emerging from the decision were:

➤ Foreign state immunity was waived

Spain was found to have waived its foreign state immunity, despite the lack of any express wording in the ICSID Convention to this effect. Spain had argued that it was an established international law principle that waiver of state immunity via a treaty can only ever be express, not implied. Given that Australian statutes will be interpreted consistently with international law, so far as possible, Spain argued the same approach should be followed when considering waiver of immunity under the Foreign States Immunities Act, s 10.

The High Court rejected this argument:

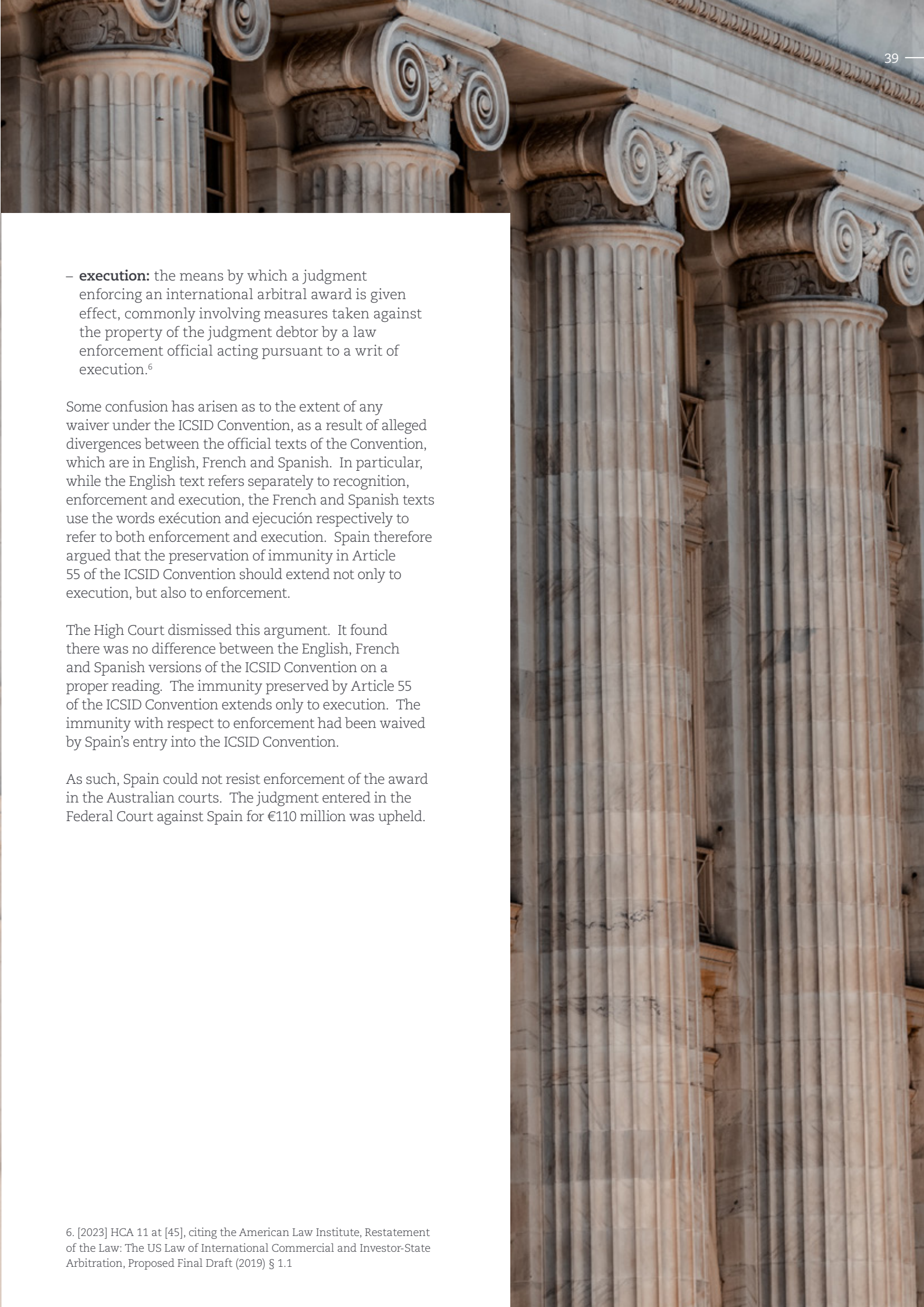
- it concluded the international law principle was less absolute, requiring only that the waiver be "*derived* from the express words" of the treaty, which may be by implication, where the implication is clear from the words used and the context (at [25] & [26]);
- once the international law principle was properly understood, there was no reason to exclude the possibility of implied waiver as a matter of Australian domestic law, pursuant to the *Foreign States Immunities Act*, s 10;
- however, "a high level of clarity and necessity are required before inferring that a foreign State has waived its immunity in a treaty because it is so unusual, and the consequence is so significant" (at [28]);
- in this case, the High Court found this demanding standard was met – the waiver was "unmistakeable" (at [29]).

➤ Waiver included recognition and enforcement

The High Court found that Spain's waiver of immunity extended to both recognition and enforcement of a valid and binding ICSID award in the Australian courts.

The High Court's analysis distinguished between 3 concepts (which it said had been used in "vague, overlapping and even interchangeable senses" in some international arbitration contexts):

- **recognition:** the court's determination that an international arbitral award is entitled to be treated as binding;
- **enforcement:** the legal process by which an international award is reduced to a judgment of a court that enjoys the same status as any judgment of that court; and



– **execution:** the means by which a judgment enforcing an international arbitral award is given effect, commonly involving measures taken against the property of the judgment debtor by a law enforcement official acting pursuant to a writ of execution.[6]

Some confusion has arisen as to the extent of any waiver under the ICSID Convention, as a result of alleged divergences between the official texts of the Convention, which are in English, French and Spanish. In particular, while the English text refers separately to recognition, enforcement and execution, the French and Spanish texts use the words exécution and ejecución respectively to refer to both enforcement and execution. Spain therefore argued that the preservation of immunity in Article 55 of the ICSID Convention should extend not only to execution, but also to enforcement.

The High Court dismissed this argument. It found there was no difference between the English, French and Spanish versions of the ICSID Convention on a proper reading. The immunity preserved by Article 55 of the ICSID Convention extends only to execution. The immunity with respect to enforcement had been waived by Spain's entry into the ICSID Convention.

As such, Spain could not resist enforcement of the award in the Australian courts. The judgment entered in the Federal Court against Spain for €110 million was upheld.

6. [2023] HCA 11 at [45], citing the American Law Institute, Restatement of the Law: The US Law of International Commercial and Investor-State Arbitration, Proposed Final Draft (2019) § 1.1

Next steps

The decision was not concerned with any attempt to execute against assets of the Spanish Government in Australia. Any claim by Spain to immunity from execution remains unaffected. While foreign states are generally immune from execution of court judgments in Australia,[7] there are exceptions in the Foreign States Immunities Act, including for execution against commercial property (s 32). It remains to be seen whether the investors are successful in obtaining execution against Spain of the Federal Court's enforcement orders.

Key takeaways

There are several important points to note arising from the decision:

- Parties dealing with foreign governments or state-owned entities, or who are reliant upon foreign governments for successful execution of their projects, should structure their transactions carefully at the outset in order to obtain maximum protection under investment treaties.

- While the investor-state arbitration system has its critics, it is likely to remain an important source of remedies for investors engaging in international trade. Increasingly the system is being used both by and against governments to resolve controversies arising out of climate-related policies and projects.

- While the generally pro-arbitration stance of the Australian courts is well established in the field of commercial arbitration, this decision suggests the courts are also inclined to uphold the international framework for investor-state arbitration.

- Australian courts are willing to recognise and enforce valid and binding ICSID awards obtained against foreign states despite claims of foreign state immunity.

- Once enforcement orders are obtained from the Australian courts, the process of executing those orders is a separate process and foreign state immunity will still be relevant in this context (though there are exceptions which may apply).

- Investors locked out of enforcement of ECT and other investor-state awards in the European Union may increasingly look to Australia as a venue for enforcement.

7. Foreign States Immunities Act, s 30

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Notes

480

Partners

2,400

Lawyers

3,200

Legal professionals

5,000

Total staff

60+

Offices worldwide*

clydeco.com

*Includes associated offices

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