INTERNATIONAL ARBITRATION IN THE ERA OF ECONOMIC SANCTIONS

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Executive Summary

*Unilateral restrictive economic measures ("**UREM**") are a country or block of countries-based measures aimed to restrain a target country's economic relations and humanitarian well-being.*

An avalanche of national UREM programs introduced by some states against the nationals of other states as well as counter-UREM regulations, negatively affect global trade, and consequently, international commercial arbitration. Accordingly, to pursue its case in international arbitration, a party affected by UREM must negotiate an ultimate obstacle course of legal restrictions and commercial limitations, which quite often become an insurmountable impediment to "having one's day in court".

Difficulties may arise at each stage when a party instructs service providers (legal counsel, expert witness, support services), initiates arbitration proceedings and pays arbitration fees, constitutes an arbitral tribunal or brings challenges, deals with the effect of UREM on an underlying commercial contract, deals with the setting aside of an arbitral award, pursues recognition and enforcement of the arbitral award.

Having in mind the impediments inherent to institutional arbitration, ad hoc arbitration can be a viable option for UREM-affected disputes.

1. Introduction

Unilateral restrictive economic measures ("**UREM**") are a country or block of countries-based measures aimed to restrain a target country's economic relations and humanitarian well-being.

It is believed that the first known use of UREM dates to 432 BC. The economic sanctions were levied upon the town of Megara by the Athenian Empire under the Megarian Decree on a pretext of the Megarians' cultivation on land that was consecrated to Demeter and the killing of the Athenian herald who was sent to reproach Megarians. The Megarian Decree blocked Megara from trading in any port within the Delian League. According to some historians, the Megarian Decree encouraged the beginning of the Peloponnesian War which eventually led to the defeat of the Athenian Empire by Sparta.

Another remarkable historic example is Napoleon's blockade of Great Britain introduced under the Berlin Decree in 1806. The Preamble to the Berlin Decree proclaimed that "*England does not admit the right of nations as universally acknowledged by all civilized people*" and "*That this conduct in England (worthy of the first ages of barbarism,) has benefitted her, to the detriment of other nations*".[1]

The so-called Continental system imposed a blockade, forbade commerce, entry into continental ports of vessels from England and its colonies, and correspondence with the nationals of England, and permitted confiscation of English merchandise and property, being a lawful prize. One-half of the proceeds of the confiscation of the merchandise and property was used to indemnify the continental merchants for the losses which they suffered from the capture of merchant's vessels by English cruisers. The continental persons, who dealt with England were

[1] https://www.napoleon.org/en/history-of-the-two-empires/articles/the-berlin-decree-of-november-21-1806/

designated as accomplices. Finally, the Berlin Decree stipulated that it had to be considered the fundamental law of the empire.

There are different historical examples of UREM, however all of them had a common outcome. UREM not only resulted in the disruption of international trade but eventually fundamentally undermined the economic and political foundation of those who had imposed them.

According to the principle that history never repeats itself — it spirals, the XX century spiraled to a new level where the use of UREM became a tool for projecting national foreign state policies internationally. While the global economy was on the rise, UREM were imposed mainly in response to political events abroad. However, in the recent decade, due to global economic decline, fragmentation, and economic protectionism, competition for markets in international trade has intensified. Consequently, UREM have also become an instrument for projecting national economic interests outward.

Newton's third law of motion states that for every action, there is an equal and opposite reaction. In line with this law, in response to numerous UREM programs, targeted states introduced their measures to counter UREM. For example, Russia and China introduced such laws.

Today, the body of different national UREM and counter-UREM has become the Great Barrier Reef of global trade, with its dangerous currents, sharp reefs, and deceptively beautiful predators. To be able to navigate in these dangerous waters, a diligent person needs to employ a sophisticated compliance apparatus. The current situation harms global trade and consequently international arbitration.

Currently, for some persons, access to justice, from being a basic right has become nearly a privilege. Even those persons who are not yet affected by UREM have experienced delays in institutional arbitration, and as a result have started searching for alternatives.

2. The Impact of UREM on International Arbitration

An avalanche of national UREM programs introduced by some states against the nationals of other states as well as counter-UREM regulations, negatively affect global trade, and consequently, international commercial arbitration. Accordingly, to pursue its case in international arbitration, a party affected by UREM must negotiate an ultimate obstacle course of legal restrictions and commercial limitations, which quite often become an insurmountable impediment to "*having one's day in court*".

Difficulties may arise at each stage when a party:

(a) instructs service providers (legal counsel, expert witness, support services);

(b) initiates arbitration proceedings and pays arbitration fees;

(c) constitutes an arbitral tribunal or brings challenges;

(d) deals with the effect of UREM on an underlying commercial contract;

(e) deals with the setting aside of an arbitral award;

(f) pursues recognition and enforcement of the arbitral award.

Although this list is not exhaustive, the above are probably quite common for UREM-affected arbitrations. All of the above, in conjunction with the pressing deadlines in an average arbitration, clearly put one of the parties in an inferior position vis-a-vis the other party.

Instructing a legal representative

The journey begins with instructing a legal representative. For example, if an SDN is targeted by the EU, instructing a counsel in the EU may become difficult, if not impossible. Although in July 2022 the EU introduced an exemption for the provision of legal services in contentious matters,

as a matter of fact, in some jurisdictions, hiring a legal counsel remains problematic. Global business has become highly politicized and local law firms may refuse to accept instructions due to possible reputational risks.

Even if an SDN is not targeted by the EU but has been included in the U.S. UREM programs, those law firms which have a presence in the U.S., have U.S. nationals as employees or even have U.S. clients, would likely refuse from acting for the SDN.

In any event, as a first step, an SDN may approach several law firms. At this stage, the SDN informs the prospective legal counsel of its SDN status and may disclose some information about the case and identity of the counterparty. While some law firms may immediately refuse to be involved, others will carry out an internal compliance check and may eventually require obtaining a state license to represent the client. Understandably, an application for a UREM license would require disclosure of information about the parties, contract, and dispute, which on its own may harm both parties. The process may take from several weeks to several months and, as a result, the list of potential legal counsel reduces from a dozen to just a few. As the options are limited, often the choice of a legal representative is truncated, vis-à-vis the choice available to the counterparty. Eventually, it cannot be excluded that the SDN will eventually fail to instruct a qualified legal counsel.

In addition, SDNs may be subject to stricter payment terms under various UREM programs. For example, some of the UREM limit repayment terms under loans (credits) to 14 days. To avoid allegations of violation of UREM, law firms may want to ensure that their services are not credited for longer than 14 days and therefore frequently invoice SDNs. Consequently, it increases administrative work on the part of law firms and clients.

Finally, due to various restrictions imposed on the banking sector, leading to delays or impossibility to pay legal fees, instructing a legal counsel from the EU, US, and UK would likely be futile.

Instructing an expert witness

Expert witnesses (or experts) are commonly used in international arbitration to address legal, accounting, technical, and other issues. According to the 2012 International Arbitration Survey: Current and Preferred Practices in the Arbitral Process "*On average, expert witnesses are involved in two-thirds of arbitrations*."[2] Furthermore "*in the vast majority of arbitrations, expert witnesses are appointed by the parties (90%) rather than by the tribunal (10%)*" Thus, it is a predominant practice that expert witnesses are appointed by parties, not by the tribunal.

Naturally, an SDN which intends to instruct an expert mainly faces similar problems to those when instructing a legal counsel. Again, UREM may limit the pool of available candidates, and increase time and costs.

One of the common issues which may be put before legal experts is the effect of UREM on commercial contracts. For example, if U.S. UREM is at the heart of a dispute, that will require a U.S. qualified and experienced lawyer to act as an expert. Under Title 31 of the Code of Federal Regulations §589.506(a)(1), U.S. nationals are permitted to advise on compliance with the requirements of U.S. law.[3] However, §589.506(a) does not extend to expert testimony in foreign courts or arbitral tribunals on behalf of an SDN without obtaining an OFAC license. In practice, OFAC mostly denies applications for such licenses. In these circumstances, SDNs often try to instruct a non-U.S. person (not a national or a resident of the U.S.), however, who holds a U.S. law degree, has UREM-related experience, and has no conflict of interest. A search for a legal

[2] 2012 International Arbitration Survey: Current and Preferred Practices in the Arbitral Process, P.29 http://www.arbitration.qmul.ac.uk/media/arbitration/docs/2012_International_Arbitration_Survey.pdf

[3] https://www.ecfr.gov/cgi-bin/text-idx?node=pt31.3.589&rgn=div5#se31.3.589_1506

expert with such qualifications may prove to be difficult. Sometimes, the only practical solution is to dispose of party-appointed experts and ask the arbitral tribunal to appoint its expert.

The appointment of an expert witness by the tribunal may become an option should the parties agree to apply the Prague Rules on the Efficient Conduct of Proceedings in International Arbitration (2018). Article 6 of the Prague Rules provides an elaborate procedure for instructing an expert witness by the tribunal.[4]

Therefore, if an SDN envisages difficulties, it may be worth exploring with an arbitral tribunal and the opposite party at the outset of the proceedings the idea of the tribunal-appointed experts. Such a possibility is normally envisaged in the applicable arbitration rules and national arbitration laws.

Procurement of Auxiliary Services

In addition to legal and expert services, parties may also require case support services, e.g. interpreters, court reporters, providers of hearing equipment, hearing facilities, hearing bundles, and others. Although these contractors may not look like the most critical element of the arbitration process, usually they are procured as a matter of urgency, and very often not so long before the evidentiary hearing. In such circumstances, one needs to factor in additional time which will be required for supporting contractors to perform compliance checks.

To avoid delays in the proceedings, upon request of parties, an arbitral tribunal may engage directly with service providers to exclude any UREM-related issues from the picture. This is something parties and an arbitral tribunal may want to discuss when agreeing on the procedural rules set out in Procedural Order No.1.

Commencing Arbitration under the Institutional Arbitration Rules

As a general rule, to initiate the arbitral proceedings under the rules of an arbitral institute ('**AI**') a claimant must file a request for arbitration and pay a registration fee. If an AI is located in a state which has imposed UREM against the claimant, it is bound to comply with them. If an AI is not located in or connected with a state which imposed UREM, it may want to perform a compliance check to ensure that it does not manifestly violate any UREM, which may expose it to penalties or secondary sanctions of a third state. For example, U.S. Executive Orders which impose UREM are binding upon "U.S. persons" (U.S. nationals and residents). Because some of the leading European AIs have U.S. persons in their governing bodies and case management teams, it may expose them to the effect of U.S. UREM. To avoid such exposure, AIs may employ a 'ring fencing' mechanism by excluding U.S. persons from the decision-making and management of SDN-related cases. For the same reason, an AI may use the currency of a non-sanctioning state to avoid exposure to the financial system of a sanctioning state, such as payments in euros used by the ICC or in Hong Kong dollars used by HKIAC.

In 2015, the ICC, LCIA, and SCC issued a joint statement on the potential impact of EU sanctions against Russia on international arbitration administered by EU-based AIs. All three arbitration institutes concluded that "*A person or entity designated by the EU Regulations is not per se prevented from filing a request for arbitration with the ICC, LCIA or SCC.*", with the caveat that a designated person or entity is advised to inform the institution of a dispute before the request for arbitration, to enable the institutions to discuss with the parties any additional administrative requirement that needs to be fulfilled either by the parties or the institution, for example filing an application with the relevant national authorities for an exemption under the sanction regulation.[5]

[4] https://praguerules.com/prague_rules/
[5] https://sccinstitute.com/media/80988/legal-insight-icc_lcia_scc-on-sanctions_17-june-2015.pdf

The joint statement by the leading AIs surely gave some comfort to Russian companies. Indeed, the 2016 Russian Arbitration Association's Survey on the Impact of Sanctions on Commercial Arbitration ('**2016 RAA Sanctions Survey'**) revealed that although some users have already had problems with some AIs, the majority continued to place trust in institutional arbitration at large.[6] However, there were some skeptics, who questioned AI's ability to ensure sustainable administration of SDN-related disputes.

Over the years the number of skeptics grew, mainly because of their personal experience with the European AIs. The difficulties primarily related to the lengthy process of obtaining licenses to administer cases by AIs and problems with payment of the arbitration costs to AIs.

Delays in administering payments may diminish the AIs' endeavors to increase efficiency of the proceedings. Needless to say, the tools such as emergency arbitration or expedited arbitration diminish in value because delays in payments of the filing fees may preclude a party from an expedient relief.

Another important consideration is confidentiality. When seeking state permission to administer SDN-related cases, AIs disclose information about the parties, underlying contracts, and relevant information about transactions to the state authorities which are responsible for enforcement of UREM. Having in mind a high degree of subjectivity and politicization of the standards of proof on the part of UREM enforcing state bodies, the risk of penalties and secondary sanctions increases dramatically. Therefore, some parties may consider it risky to use institutional arbitration and consider alternative means of dispute resolution, such as *ad hoc* arbitration.

With that in mind, most Russian companies (also non-SDNs) have been reconsidering their traditional preferences in arbitration, which have been shaped over decades. Led by example, arbitration users from other jurisdictions also have started avoiding institutional arbitration in their new contracts. The rationale is simple, in the current circumstances, any company from any state may become a target of some UREM. Presumably, the change in the arbitration users' preferences will be visible in AIs' annual statistics in the foreseeable future.

By far, the main impediment to institutional arbitration is receiving payments of arbitration costs from SDNs. Even if a money wire is executed in a non-sanctioned currency, banks' compliance departments usually do not allow money transfers originating from or relating to SDNs. For example, a local German bank will likely refuse payment in EUR from a Russian SDN designated under the U.S. UREM (even if it is not designated under the EU UREM). The reason is simple, a bank does not want to take the risk of penalties or the risk of secondary sanctions from the U.S. authorities (OFAC). Ultimately, not having received a claimant's payment of the registration fee or arbitration costs, an AI would discontinue the arbitration according to its arbitration rules.

There have been numerous examples when AIs were unable to arrange for a bank that would accept payments from SDNs. An AI may face similar problems when returning to the parties unused funds from the arbitration costs after the case was completed. Similarly, there may be a delay in paying the arbitrators' fees if an arbitrator is a resident of a state affected by UREM.

To conclude, payment of arbitration costs is an Achilles heel of institutional arbitration. Commonly, AIs are fixed to their local banks and refuse to explore other payment options. Considering the rapid expansion of the UREM programs across the globe, UREM present a potential risk to many notable market players – there is no guarantee that a person will not be designated as an SDN in the future.

Usually, all these issues may be taken into account at the stage of drafting a contract. There is an array of contractual tools for minimizing the negative effects of potential UREM, including the

[6] https://arbitration.ru/upload/medialibrary/e1e/2016-raa-survey-on-sanctions-and-arbitration.pdf

alternative dispute resolution clauses (waterfall clauses), currency, and payment terms, which enable a party to arbitrate its future contractual claims irrespective of its SDN status.

However, there is a growing number of SDN-related cases which are hovering as a result of AIs payment problems. That raises several important questions.

First, if an AI refuses or delays case administration that involves an SDN, what is the effect on the arbitration agreement? Would the arbitration agreement become inoperable, unenforceable, invalid, or else? Consequently, can an SDN disregard the arbitration clause and pursue its claims in the court of law, and if yes, in which court? For example, Russian and Chinese counter-sanction laws permit SDNs to disregard arbitration agreements and apply to local courts as if there were no arbitration agreements in place.

Second, if an SDN-respondent intends to bring a counterclaim or a set-off claim, but the AI fails to accept the payment of arbitration fees, what is the effect on the counterclaim or the set-off claim and the arbitration agreement? In some cases, this may be resolved by shifting payment obligations onto the other party in arbitration, which is however not always an optimal solution.

Third, if an arbitration agreement is deemed to be unenforceable in connection with the agreed AI's procedures, does it make the parties' intention to arbitrate (as opposed to litigating) unenforceable too? In other words, should the parties still apply their best efforts to arbitrate their dispute, for example in an *ad hoc* setup?

Fourth, if an AI fails to administer an SDN-related case, does it amount to a breach of contract by the AI? Indeed, when the parties to an arbitration agreement consent to refer their disputes to a particular AI, they accept the AI's contract terms expressed in its arbitration rules. According to its own arbitration rules, the AI guarantees that it will administer the case.

Fifth, if an AI fails to administer an SDN-related case, does it lead to the AI's contractual liability? Most arbitration rules contain a limitation of liability provisions, however, such provisions usually concern "*any act or omission in connection with the arbitration*".[7] Under many arbitration rules, arbitration commences after the AI receives a request for arbitration and the full amount of the registration fee. Formally speaking, at any time before the commencement of arbitration (including before payment of the registration fee), there is no arbitration. Therefore, it is not obvious whether the limitation of liability provisions in the arbitration rules encompasses the pre-arbitration liabilities of the AIs.

In practice, there have been only a few examples when parties to arbitrations brought liability claims against AIs[8] and even fewer examples when the parties succeeded[9]. Notwithstanding that, this avenue remains available to the dissatisfied parties.

Each of these questions requires the parties' consideration at the time of drafting an arbitration agreement. As noted above, to some extent the problem is resolved through 'waterfall' clauses, according to which parties may agree on several possible options of AIs, and if one option does not work, they move to another. Such multi-tier arbitration clauses require careful drafting to avoid parallel proceedings. Another solution is to opt for *ad hoc* arbitration, which is more flexible than institutional arbitration. Also, for these reasons, in recent years, *ad hoc* has gained popularity.

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[7] See, Article 41 of the ICC Rules of Arbitration (2021); Article 31 of the LCIA Arbitration Rules (2020); Article 52 of the SCC Arbitration Rules (2017).

[8] *RSM Production Corporation v World Bank Group et al*, Case number: 1:13-cv-00783 (D.D.C.); Cour de cassation, Première chambre civile, 22 mars 2023, n° 21-16.238, *Kraydon Ltd c/ Chambre de commerce internationale de Paris (CCI).*

[9] Tribunal de grande instance de Nanterre (1re Ch.), 1er juillet 2010, *Société Filature Française de Mohair c/ Fédération Française des Industries Lainière et Cotonnière.*

As to the AIs, there is a possibility to seek a license or an advisory opinion from the relevant state bodies, that would enable them to administer the UREM-related cases.

The constitution of the Arbitral Tribunal

The constitution of the arbitral tribunal may also present difficulties in SDN-related cases. Some arbitrators may hesitate to receive nominations from SDNs, especially if an arbitrator's country imposed UREM on an SDN. For the same reason, an agreed chairperson may also refuse to accept the appointment. That may limit the pool of suitable candidates and slow down the process. The situation may aggravate if the applicable substantive law is the law of the sanctioning state, but suitable candidates from that state would not agree to accept a nomination from the SDN. In that situation, it is hard to ensure that the parties will be on an equal footing in the arbitration.

The 2016 Russian Arbitration Association ("**RAA**") Sanctions Survey revealed that arbitrators were generally ready to accept nominations from the SDNs. The results included answers from 99 arbitrators, 62 of whom originated from the states which levied UREM against Russian companies, and 37 originated from other nations.

The survey revealed that if the seat of arbitration was in the sanctioning state, 77 arbitrators would accept a nomination as arbitrator from an SDN. Only 8 arbitrators would refuse and 15 did not answer. To sum up, 77% of all interviewed arbitrators would accept a nomination from an SDN if the seat of arbitration was in the sanctioning state.

However, if the seat of arbitration was outside the sanctioning state,72 arbitrators would accept a nomination as arbitrator from an SDN. Only 7 arbitrators would refuse and 21 did not reply. To sum up, 72% of all interviewed arbitrators would take a nomination from an SDN if the seat of arbitration was not in the sanctioning state.

Although the results of the 2016 RAA Sanctions Survey gave some hope, the constitution of the arbitral tribunal presents difficulties in practice. This is especially true in the current circumstances.

As a practical consideration, parties may avoid choosing the law of a state which has imposed the UREM as the substantive law of a contract. Similarly, parties may want to avoid selecting a seat of arbitration in a sanctioning state or a state which may potentially impose UREM in the future.

The Effect of UREM on Commercial Contracts

An arbitral tribunal that considers an SDN-related case may expect to be asked to rule on the issues of public policy, force majeure, hardship, changed circumstances, validity, and enforceability of a commercial contract affected by UREM.

Although some of these issues may be agreed upon in the contract, many other issues depend on the applicable substantive law and its imperative norms. Therefore, the contents of the imperative norms shall be borne in mind when drafting a contract and arbitration clause. One such norm to bear in mind is Article 11 of the Council Regulation (EU) No. 833/2014 of 31 July 2014 concerning restrictive measures because of Russia's actions destabilizing the situation in Ukraine, which reads as follows:

> *1. No claims in connection with any contract or transaction the performance of which has been affected, directly or indirectly, in whole or in part, by the measures imposed under this Regulation, including claims for indemnity or any other claim of this type, such as a claim for compensation or a claim under a guarantee, notably a claim for extension or payment of a bond, guarantee or indemnity, particularly a financial guarantee or financial indemnity, of whatever form, shall be satisfied, if they are made by*:

(a) entities referred to in points (b) or (c) of Article 5, or listed in Annex III;

(b) any other Russian person, entity or body;

(c) any person, entity, or body acting through or on behalf of one of the persons, entities or bodies referred to in points (a) or (b) of this paragraph.

Despite the passive voice employed by Article 11 ("*no claims shall be satisfied*"), one may interpret the language as prohibiting all EU-based AIs and arbitrators to satisfy any claims brought by or on behalf of an SDN and even broader – by "*any other Russian person, entity or body*". Eventually, Article 11 of the EU Regulation harms both – SDN users and European providers of arbitration services.

Given the difficulties that a national applicable law may entail, (e.g. preventing an SDN from instructing legal representatives, experts, and service providers, nomination of arbitrators) parties may consider choosing the applicable law of a state which has not imposed and will unlikely impose UREM in the future. Alternatively, parties may fully exclude the application of national laws and rediscover *lex mercatoria*, as an autonomous legal system. It could be the UNIDROIT Principles of International Commercial Contracts, the Principles of European Contract Law (PECL), or sets of other delocalized legal norms (FIDIC, INCOTERMS, etc.).

Setting Aside and Recognition and Enforcement of Arbitral Awards

Validity and enforceability of an arbitral award is the final stop before collecting the debt. A state judge has to decide, *ex officio*, whether the arbitral award complies with the "public policy" of a particular state, and more precisely with its UREM-related restrictions. A lot has been said about public policy, but the following quotes describe it in the most concise yet comprehensive manner.

> *Public policy does not admit to a definition and is not easily explained. It is a variable quantity; it must vary and does vary with the habits, capacities, and opportunities of the public.*[10]
>
> *It is impossible to say what the opinion of a man or a Judge might be as to what public policy is.*[11]
>
> *Public policy is a very unruly horse, and when once you get astride it you never know where it will carry you.*[12]

Indeed, it is impossible to say what the opinion of a judge might be as to what public policy is, especially when he or she deals with UREM. After all, the question of enforcement may be just a theoretical dilemma, because in the current circumstances, only a few SDNs may successfully reach the stage of recognition and enforcement of arbitral awards (keeping in mind all the obstacles during the arbitration proceedings).

3. Can licenses to AIs level the playing field?

On 17 October 2022, the LCIA announced that the Office of Financial Sanctions Implementation of the HM Treasury had issued a General Licence for cases administered by the LCIA under the LCIA Rules.[13] The LCIA informed that "*The General Licence will cover all cases administered based on the LCIA Rules, as opposed to cases where the LCIA merely acts as fundholder or performs services in cases conducted on the basis of the UNCITRAL Rules, which will require individual licences. The General Licence applies to cases administered on the basis of the 2020*

[10] Kekewich, J., Davies v. Davies (1887), L. R. 36 C. D. 364; see also Egerton v. Earl Brownlow, 4 H. L. C. 1.
[11] Jessel, M.R., Besant v. Wood (1879), L. R. 12 C. D. 620.
[12] Burrough, J., Richardson v. Mellish (1824), 2 Bing. 252; quoted by Lord Bramwell in Mogul Steamship Co.;. McGregor, Gow and others, 66 L. T. Rep. 6.
[13] https://www.lcia.org/News/lcia-procures-a-comprehensive-lcia-specific-general-licence-re.aspx

Rules, as well as the 2014 and 1998 Rules. It covers payments to the LCIA by Designated Persons (DPs), companies owned and controlled by DPs or their legal representatives and extends to registration fees, deposits, arbitrator fees and expenses and LCIA charges, as well as fees and expenses of tribunal secretaries and experts appointed by the tribunal, pursuant to the LCIA Schedule of Arbitration Costs. The Publication Notice further confirms that the LCIA may receive substitute deposit(s) from non-DPs who are party to the arbitral proceedings to allow the arbitration to proceed where a DP or company owned or controlled by a DP fails to make the payment for arbitration costs. While the LCIA does not require a licence to return funds to non-designated parties, the General Licence does not extend to restitution payments to DPs, which will require individual licences, and equally does not cover the DPs' other payment obligations such as payments to their legal representatives or third parties for services related to the arbitration."

Although it seems to be a sensible solution currently, it gives little comfort to the users of arbitration. That is because paragraph 9 of the General License stipulates that HM Treasury may vary, revoke or suspend the General Licence at any time. As they say, you cannot catch old birds with chaff. Therefore, it will take quite some time before the leading arbitration jurisdictions and AIs will regain their reputation as reliable seats for UREM-related cases. Currently, it seems unfeasible that, for example, Russian parties (whose share in various European AIs amounted to up to 20-30% of the casework from time to time) will return to the European AIs. Furthermore, Asian, African, and Latin American parties given the ongoing and upcoming trade wars and new UREM programs already look at the leading AIs with a dash of skepticism.

4. *Ad hoc* arbitration as an alternative

As can be seen, some of the irreconcilable difficulties in pursuing a claim in institutional arbitration arise from the inability of some of the AIs to administer cases duly and expeditiously.

Consequently, end-users may be in search of alternatives to institutional arbitration.

One such alternative is *ad hoc* arbitration. *Ad hoc* arbitrations are arranged solely between the arbitrators and the parties. In *ad hoc*, the parties are not bound by any institutional limitations and are free to design the procedure and fundholding most conveniently.

The interviewees of the 2021 Study by the Queen Mary University of London "*valued the procedural flexibility offered by ad hoc arbitration, which they felt enhanced party autonomy compared to institutional arbitration*."[14]

What are the advantages of *ad hoc* compared to institutional arbitration?

(a) The parties and tribunal may decide on an appropriate remuneration model.

The majority of AIs' schedule of arbitration costs is based on the *ad valorem* model, i.e., arbitration costs are fixed according to a scale of costs based on the monetary value of the claims (e.g., ICC, SCC, VIAC, etc). In other AIs, arbitration costs are calculated according to the hourly rates of the secretariat and arbitrators (e.g., LCIA). Only a handful of AIs have the option of paying arbitral tribunals' fees by hourly rate or by reference to an *ad valorem* fee scale (e.g., HKIAC).

In *ad hoc*, depending on the value and complexity of the dispute the parties and tribunal may agree on the most economically sound model of arbitration costs. For example, for non-complex but high-value disputes it may be sensible to use the hourly-based model. In the end, the parties' arbitration payments may be significantly lower than if they used the *ad valorem* model. Similarly, for complex disputes but with an insignificant monetary value the model based on the

[14] 2021 International Arbitration Survey: Adapting arbitration to a changing world. P.9 https://arbitration.qmul.ac.uk/media/arbitration/docs/LON0320037-QMUL-International-Arbitration-Survey-2021_19_WEB.pdf

hourly fees may ensure fair compensation to the arbitrators. However, if the arbitrators deal with a complex dispute of a high monetary value, it may be fair to use the *ad valorem* model.

Furthermore, when opting for the *ad valorem* model, the parties and tribunals may agree on a specific schedule of fees. It is not uncommon to link arbitrators' fees in *ad hoc* arbitrations to one of the AIs' schedules of fees that the parties deem appropriate for a particular case.

(b) The parties and tribunal may pre-agree on the arbitrators' fees and payment terms.

Unlike in institutional arbitration, in *ad hoc,* the parties and tribunal may also agree to cap the arbitration costs or on various adjustment models which assist to achieve the most economical way of resolving the dispute. In addition, they may agree on whether payments are made as a lump sum or installments. This level of flexibility is usually not available in institutional arbitration.

(c) No additional fees for the case administration are charged.

Arbitration costs in institutional arbitration comprise a fixed filing fee, administrative costs, and arbitrators' fees. The filing fee and administrative costs may amount to 10-15% of the entire arbitration costs. In *ad hoc*, these may be abandoned, which enables the parties to save costs.

(d) More options for alternative currencies and payment methods of arbitration costs.

Somewhat nearly unimaginable for institutional arbitration, in *ad hoc*, the parties may propose to use alternative currencies, banks, and payment methods. There may be used escrow accounts, bank guarantees, third-party guarantees, bonds, and other alternative payment instruments. In terms of the currency of payments, the parties may agree on the currencies that are not affected by UREM and that they may be paid to the banks in a neutral jurisdiction. The parties may also propose to pay in digital or cryptocurrencies.

(e) More options for fundholding

Ad hoc tribunals, in consultations with the parties, may freely choose between different fundholding models. They may elect a person who will hold the funds (a private or legal person), the location of fundholding and in which banks the funds may be deposited.

(f) Stricter confidentiality

In institutional arbitration information about a dispute is exposed to a wider group of persons, such as the members of the AI's case management team, compliance department, IT personnel, the board as well as the arbitral tribunal. In *ad hoc* arbitration, the information would not leave the perimeter of the arbitral tribunal and its secretary.

(g) Less exposure to UREM

An AI, because of its geographical location, the jurisdiction of incorporation, and nationalities of its personnel and the board, may be bound to report information about the parties and nature of the dispute to the state authorities that imposed certain UREM. This alone may preclude the parties from seeking a resolution of their dispute under the rules of an AI.

In contrast, in *ad hoc*, the parties may appoint the members of the tribunal who have no exposure to UREM and therefore have no reporting obligations. Not only does it ensure confidentiality, but also substantially reduces regulatory risks to both parties and duration of the proceedings.

(h) Fewer time constraints

One of the key performance indicators that AIs employ is the duration of the arbitral proceedings. It is common that in the annual statistics, AIs report on the average duration of cases administered under their rules. To achieve procedural efficiency, AIs strive to reduce case

duration by imposing rather strict deadlines on the parties for submitting their replies to the requests for arbitration, for appointment of arbitrators, for payments of arbitration costs, and ultimately, for rendering the arbitral awards.

However, longer procedural deadlines, especially at the outset of the arbitral proceedings, may be particularly important when dealing with SDNs. This is because an SDN may require a longer time for instructing a legal team, appointing an arbitrator, making payments, etc. Sometimes, when a party addresses these issues to an AIs, in response, the AI denies the extension of time by noting something along these lines: "*The answer to the request for arbitration does not have to state the entire position of the party. The Respondent will have an opportunity to address its position in detail in its subsequent submissions*". However, it shall be up to the party to decide on the case strategy and whether the party wishes to present the main points of its position already at the beginning, or a later stage of arbitration. Led by the saying that "*You never get* a *second chance* to *make a good first impression*" a party may wish to submit a more elaborate position already in the reply to the request for arbitration rather than limiting itself to a truncated technical reply.

5. Conclusion

Having in mind the issues discussed above, *ad hoc* arbitration seems to be a viable option for UREM-affected disputes.

Indeed, according to the 2006 Study by the Queen Mary University of London 76% of corporations opt for institutional arbitration and 24% opt for *ad hoc* proceedings.[15] Furthermore, the 2008 Study by the Queen Mary University of London demonstrated that 86% of arbitration awards rendered arose from institutional arbitration, and 14% were made in ad hoc proceedings.[16]

Although the AIs are leading the development of international arbitration, they appear to be unprepared for the changing circumstances. Gradually, *ad hoc* arbitration is becoming a quiet winner in the arbitration race, offering a tailor-made approach to each case, and consequently, the so needed efficiency, flexibility and integrity of the proceedings.

As ever before, international arbitration needs to be indifferent towards politics and shall damper their negative effects on global trade. Otherwise, it will eventually lose the parties' trust. *Ad hoc* arbitration may be a way forward to ensure the future of international arbitration.

[15] International arbitration: Corporate attitudes and practices 2006. P.12 https://arbitration.qmul.ac.uk/media/arbitration/docs/IAstudy_2006.pdf

[16] International Arbitration: Corporate attitudes and practices 2008. P. 15 https://www.pwc.co.uk/assets/pdf/pwc-international-arbitration-2008.pdf