

Siemens Russia case: the risks of managing sanctions compliance through contracts

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In two disputes concerning the delivery of Siemens gas turbines to Crimea in violation of European sanctions, the Moscow Commercial Court has confirmed the validity of the contracts that enabled the delivery of Siemens turbines to Crimea. The court deemed those transactions lawful and denied the request to return the turbines to Siemens. It also noted that invalidation of the contracts would mean de jure application of EU economic sanctions which would clearly violate the public order and damage the sovereignty of the Russian Federation. The same court and the appellate court had previously rejected Siemens' request to impose an injunction on their installation in the EU-sanctioned territory. This case illustrates the potential risks that European companies face when conducting business in Russia through local subsidiaries. It also highlights the limitations of contractual solutions aimed at securing compliance with the sanctions applicable to those European companies.

Following the annexation of the Autonomous Republic of Crimea and Sevastopol by Russia in March 2014, the European Union introduced economic sanctions targeting the annexed region ([Council Regulation No 692/2014](#)). These economic sanctions, in particular, prohibit selling, supplying, transferring, or exporting of goods and technology suited for use in the energy sector to Crimean companies or for use in Crimea. These restrictions apply to companies incorporated in any EU member state, as well as to any company which does all or part of its business within the EU. These sanctions hindered Russia's construction of two power plants in Crimea; projects of great significance for Russia from strategic, political and reputational standpoints. However, the design of the power plants specifically included the use of Siemens gas turbines; alternative turbines could not be used without substantial alterations to the project.

In March 2015, open joint-stock company Technopromexport (TPE OJSC) – an affiliate of the Russian state-owned conglomerate Rostec – entered into an agreement with a Siemens joint venture based in St Petersburg (Siemens Gas Turbines Technologies LLC, Siemens Russia) for the sale and purchase of gas turbines. The agreement provided that the turbines had to be produced by Siemens Russia, and that they were intended to be used for the construction of a power plant in the Taman peninsula in the south of Russia, which is only 16 km away from Crimea. These provisions aimed to mitigate the risk that Siemens would be in violation of European sanctions against Crimea. In October 2015, TPE OJSC resold the gas turbines to another Rostec-affiliated company – Technopromexport LLC (“TPE LLC”) – in charge of the construction of power plants in Crimea. The latter transaction became public in July 2017 when Reuters [reported](#)

that the Siemens gas turbines were about to be installed in Crimea.

Litigation in Russian courts

After Siemens discovered that the gas turbines had ended up in Crimea, in violation of the initial agreement with Siemens Russia, both Siemens Russia and Siemens AG (Siemens Germany) brought two lawsuits before the Moscow Commercial Court. In both legal proceedings, Siemens asked the court to invalidate the sequence of transactions that resulted in the gas turbines being delivered to Crimea contrary to the will and without the knowledge of Siemens Russia. The companies argued that Siemens Russia concluded the initial sale and purchase agreement under the impact of “sufficient delusion and fraud”. These circumstances constitute grounds for voiding contracts under Russian law. The invalidation of the agreements which facilitated the transfer of gas turbines to Crimea would lead to full restitution and the return of the turbines to Siemens Russia. In addition, Siemens Germany requested the court to seize the gas turbines and impose an injunction on their installation.

The Moscow Commercial Court rejected both lawsuits, having already denied Siemens' request for interim measures. Siemens' subsequent appeal of the denial of interim measures was also rejected.

In its [21 December 2017 judgment](#), the court confirmed that the geographic limitations in the relevant agreement stipulating where the turbines could be used, were lawful, even if their only purpose was to ensure compliance with European sanctions against Russia. However, in its [17 January 2018 judgment](#), the court noted that, as a Russian legal entity, Siemens Russia had no obligation to comply with the European sanctions. Notably, the court found that the main consequence of granting Siemens' claims would be de jure application of economic sanctions introduced by the European Union on the territory of the Russian Federation. This, in the court's opinion, would damage the sovereignty of the Russian state and thus “clearly contradict” the foundations of public order of the Russian Federation.

Siemens Russia has filed an appeal to this judgment, and a hearing is scheduled for 1 March 2018.

Lessons

The Siemens Russia case illustrates the risks European companies face when conducting business in Russia, either directly or through local subsidiaries.

Imposing adequate contractual limitations and obligations on your counterparty to mitigate the risk of non-compliance with applicable sanctions remains a compliance measure widely recognised by enforcement authorities. However, the Siemens case demonstrates that these measures alone only offer a limited scope of protection. This is especially relevant in a politically sensitive dispute touching upon the sovereignty of a sanctioned country. Although the Russian judiciary is particularly prone to political influence, other jurisdictions targeted by sanctions imposed by foreign states or entities are likely to be similarly protective of their legal and public order.

For this reason, conducting a due diligence investigation of all

transactions, including all relevant parties and the end use or end user of the goods or services involved, is ever more important. It is also crucial to pay close attention to, and act on, transactions which raise 'red flags', including the geographic proximity of the destination of goods to the sanctioned territory.

It is unclear whether German authorities are currently investigating the Siemens case, or if they intend to do so in the future. We will keep you informed of the latest developments.
