

White Collar Defense and Investigations Alert



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UK Court of Appeal Comments on UK Sanctions Ownership and Control Test

On 6 October 2023, the UK Court of Appeal (the **Court of Appeal**) delivered its judgment in *Mints v. PJSC National Bank Trust and PJSC Bank Otkritie*.¹ In its decision, the Court of Appeal confirmed that English courts can enter judgment in favour of designated persons and that the Office of Financial Sanctions Implementation (**OFSI**), the UK sanctions authority, can license certain litigation-related costs orders.

The Court of Appeal also gave its view on the ownership and control test under UK sanctions.² While the court's comments were nonbinding (*i.e., obiter*), the court suggested that the “control” element of the test should be interpreted broadly, such that entities in which a UK designated person “calls the shots” are subject to a UK asset freeze. As detailed below, the UK government is exploring options to address the statements made by the Court of Appeal.

Background

The case concerned a US\$850 million claim brought by two Russian banks — National Bank Trust and Bank Otkritie (together, the claimants) — against Russian businessman, Boris Mints, and his three sons (together, the defendants), alleging a conspiracy to enter into uncommercial transactions. On 28 February 2022, after the case had commenced, Bank Otkritie was designated as a blocked entity on the UK sanctions list and became subject to an asset freeze.

The defendants applied for a stay of proceedings on the grounds that the claim was impacted by UK sanctions. In particular, the defendants argued that entering judgment for the claimants would be prohibited by UK sanctions and that allowing the proceedings to continue while sanctions remained in force against Bank Otkritie would cause serious prejudice to the defendants because, among other things, the claimants could not lawfully satisfy adverse costs orders. The High Court dismissed this application, and the defendants appealed the decision.

¹ [2023] EWCA Civ 1132.

² In addition to individuals and entities listed on the UK's Consolidated List of Financial Sanctions Targets, UK financial sanctions apply to entities that are owned or controlled, directly or indirectly, by a designated person.

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The Court of Appeal said that the defendants' appeal raised the following questions:

- **The "entry of judgment" issue:** Can an English court lawfully enter judgment for a designated person?
- **The "licensing" issue:** Can OFSI licence ancillary litigation orders (including the payment by a designated person of adverse costs orders)?
- **The "control" issue:** Does a designated person "control" an entity where the entity is not his/her personal asset, but the designated person is able to exert influence over it by virtue of the person's political office?

In relation to the control issue, the defendants argued that, although National Bank Trust was not individually designated, it was subject to an asset freeze by virtue of its "control" by at least two designated persons, namely Vladimir Putin (Mr. Putin) and Elvira Nabiullina (Ms. Nabiullina), the governor of the Central Bank of the Russia Federation (the **Central Bank**).³ In particular, the defendants argued that the extension of sanctions to the National Bank Trust was logical, given that any recoveries made in the proceedings would be paid to the Central Bank, which is required under Russian law to transfer 75% of its profits to the federal budget of the Russian Federation.

Judgment

The Court of Appeal upheld the High Court's decision and dismissed the defendants' appeal.

The "Entry of Judgment" Issue

The Court of Appeal held that entering a judgment for a designated person was not prohibited by UK sanctions because the judgment did not "make funds available" to a designated person, which would breach Regulation 12 of the Russia (Sanctions) (EU Exit) Regulations 2019 (the **Regulations**).⁴ Specifically, the Court of Appeal considered that "entering the judgment and simultaneously creating the judgment debt which constitutes a fund cannot be aptly described as making the fund available"⁵ because the wording in the Regulations contemplates making available a fund that preexists. By contrast, in the *Mints* case, the "fund" would not come into existence until a judgment was entered by the court. On this basis, the court making its judgment could not itself be within scope of the asset freeze prohibitions under the Regulations. The Court of

Appeal added that the words "make funds available" were "not apt to describe the exercise by the court on one of its prime judicial functions in administering justice, of entering judgment on a valid cause of action."⁶

The Court of Appeal also disagreed with the defendants' argument that a cause of action was an economic resource, and that obtaining judgment therefore resulted in the claimants exchanging an economic resource for funds (*i.e.*, the judgment debt), which would breach Regulation 11(5) of the Regulations. Regulation 11(1) prohibits dealing with funds or economic resources owned, held or controlled by a designated person. Regulation 11(5)(b) states that a person "deals with" economic resources if the person uses the economic resource in exchange for funds, goods or services. The Court of Appeal determined that entry into judgment did not involve an "exchange" within the meaning of Regulation 11(5) because the court would not receive anything in exchange for the cause of action.⁷

The Court of Appeal also held that, even if entering a judgment was prohibited by UK sanctions, granting a stay of proceedings would not be appropriate because the court could enter a declaratory judgment or judgment on liability with quantum deferred.⁸ The court considered that such a judgment would not be either making funds available to the designated person or dealing with a fund or economic resource, and would also accord with the principle of legality, which requires that a provision be interpreted as authorising only such intrusion as is reasonably necessary to fulfil the objective of the provision in question.

The "Licensing" Issue

The Court of Appeal held that OFSI could licence all the following litigation-related orders:

- Payment of an adverse costs order by a designated person.
- Satisfaction of an order for security for costs by a designated person.
- Payment of any damages by a designated person that might be awarded in respect of the cross-undertakings in damages.
- Payment of a costs order in favour of a designated person.

The "Control" Issue

The Court of Appeal acknowledged that, having found in favour of the claimants on the first two issues, ruling on the control issue was not necessary. Nevertheless, the court noted that the issue

³ National Bank Trust is a 99%-owned subsidiary of the Central Bank.

⁴ Regulation 12 prohibits persons from making funds available, directly or indirectly, to a designated person if the person knows or has reasonable cause to suspect that they are making the funds available.

⁵ [2023] EWCA Civ 1132, para. 201.

⁶ *Ibid*, para. 202.

⁷ *Ibid*, para. 208.

⁸ *Ibid*, para. 212.

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was “fully argued” and of “general significance,”⁹ and therefore addressed it on an *obiter* basis.

The Court of Appeal first considered the two conditions for establishing ownership and control of an entity, as outlined in Regulation 7 of the Regulations:

- that a person, directly or indirectly, holds more than 50% of the shares or voting rights in the entity, or has the right to appoint or remove a majority of the board of directors (the **First Condition**),¹⁰ and
- that it is reasonable, having regard to all the circumstances, to expect that the designated person would (if they chose to) be able, in most cases or in significant respects, by whatever means and whether directly or indirectly, to achieve the result that the entity’s affairs are conducted in accordance with their wishes (the **Second Condition**).¹¹

The Court of Appeal considered that the Second Condition was drafted “in wide terms,” such that it did “not have any limit as to the means or mechanism by which a designated person is able to achieve the result of control.”¹² Therefore, the Court of Appeal rejected the argument that the Second Condition was limited to a person acting in a personal capacity and, contrary to the High Court’s decision, said that the political office exercised by a designated person was relevant to the control test. In particular, the Court of Appeal noted that if a designated person’s political office were not relevant to the test, that would have been expressly addressed in the legislation.¹³

Ultimately, the Court of Appeal determined that the “clear wording” of Regulation 7 covers all companies in which a designated person “calls the shots.”¹⁴ With that in mind, and having concluded that the political office exercised by a designated person was relevant to control, the Court of Appeal considered that National Bank Trust was controlled by Mr. Putin and Ms. Nabiullina.

Takeaways

The Court of Appeal’s interpretation of Regulation 7 has the potential to significantly broaden the ownership and control test for UK sanctions. The Court of Appeal acknowledged that its interpretation could lead to the “absurd” consequence that Mr. Putin “could be deemed to control everything in Russia.”¹⁵

⁹ *Ibid*, para. 225.

¹⁰ Regulation 7(2) of the Regulations.

¹¹ Regulation 7(4) of the Regulations.

¹² [2023] EWCA Civ 1132, para. 229.

¹³ *Ibid*, para. 231.

¹⁴ *Ibid*, paras. 229 and 232.

¹⁵ *Ibid*, para. 233.

The Court of Appeal considered that this consequence did not arise from giving the Regulations their “clear and wide meaning,” but from the UK government’s subsequent decision to designate Mr. Putin “without having thought through the consequences that ... Mr.[.] Putin is at the apex of a command economy.”¹⁶

The Court of Appeal’s interpretation of the control test could lead to significant uncertainty for those interacting with Russian entities, particularly state-owned entities. Subject to any challenge submitted to the Supreme Court (which we understand the defendants may have sought permission for), the Court of Appeal’s view, albeit *obiter*, is currently the highest judicial interpretation of the control test. Although any Supreme Court challenge is likely to focus on the entry of judgment and licensing issues, the Supreme Court may decide to address the Court of Appeal’s *obiter* comments regarding the control test.

The Court of Appeal’s judgment made clear that amending the wording of the Regulations would be the job of “the executive and Parliament,” and whether this ruling leads to any legislative change or further guidance from the UK government remains to be seen. On 16 October 2023, the UK Foreign Commonwealth & Development Office (**FCDO**) released a statement noting that the government was carefully considering the judgment and exploring the options available to clarify the position on the control test. The statement added that (i) the FCDO would designate a public body (where possible) at the same time as designating a public official if the FCDO considered that the relevant official was exercising control over the public body, and (ii) there is “no presumption on the part of the Government that a private entity based in or incorporated in Russia or any jurisdiction in which a public official is designated is in itself sufficient evidence to demonstrate that the relevant official exercises control over that entity.”

* * *

This client alert is for informational purposes only and does not constitute legal advice. Complex assessments often have to be made as to which sanctions regime applies in any given instance, given the multinational touch points of many entities and individuals. In that regard, given the complex and dynamic nature of these sanctions regimes, there may be developments not captured in this summary. Moreover, while the summary was accurate when written, it may become inaccurate over time given developments. For all of these reasons, you should consult with a qualified attorney before making any judgments relating to sanctions, as there are potentially severe consequences of failing to adhere fully to sanctions restrictions.

¹⁶ *Ibid*.

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