Investment Treaties and the Russian Federation: Baiting the Bear?

Noah Rubins and Azizjon Nazarov[1]

In July 2004, the Russian oil giant Yukos was charged with tax code violations. The ensuing court proceedings resulted in the imprisonment of Yukos' former chief, Mikhail Khodorkovsky, tax assessments of billions of dollars and the liquidation of the company's assets. Many of Yukos' most important operating assets were acquired at auction by Russian state-owned companies. Whatever the merits of the tax investigation, the move against Yukos was widely viewed as politically motivated.[2] In response to these events, a Cypriot corporate shareholder of Yukos, known as Group Menatep, stated publicly that it would challenge the legality of the auction on an international level.[3] In 2005, Menatep filed a US$28 billion arbitration claim against the Russian Federation under the Energy Charter Treaty (ECT), a European multilateral agreement designed to protect and encourage investment in the energy sector. It was soon followed by other Yukos shareholders from around Europe.[4] What are these claims, and how did these investors gain access to an international forum for the resolution of their dispute with the Russian Federation Government? And do they have any chance of success?

The answer to these questions begins in 1959, when West Germany and the Islamic Republic of Pakistan signed the very first modern treaty on the encouragement and mutual protection of investments.[5] Today, at least 2,400 such international agreements have been signed, spanning the entire world. While these treaties differ in a range of important ways, nearly all modern bilateral investment treaties (BITs) share one characteristic that makes them

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1 Noah Rubins is Counsel, Freshfields Bruckhaus Deringer, Paris. Azizjon Nazarov is Senior Lecturer, Westminster International University, Tashkent, Uzbekistan.

2 *Spanish financial investors initiate arbitration against Russia over Yukos*, IISD Investment Treaty News (ITN), 27 April 2007.

3 *Menatep's Yukos claim is largest in investment treaty history, others in offing?* IISD Investment Treaty News, 22 February 2005.

4 *Yukos Universal Ltd (UK – Isle of Man) v Russian Federation*; *Hulley Enterprises Ltd (Cyprus) v Russian Federation*; *Veteran Petroleum Trust (Cyprus) v Russian Federation.*

5 For more general information about investment treaties and recourse to international arbitration, see Noah Rubins and Stephan Kinsella, *International Investment, Political Risk, and Dispute Resolution* (2005), particularly Chapters 6 and 7.

an unusual tool in international law. They allow private individuals and companies from each of the contracting states, in certain circumstances, to submit international arbitration claims directly against the other contracting state, if investments within the territory of that state have been subjected to measures that contravene BIT standards of protection.[6] Most treaties offer investors a menu of arbitration options, most commonly the World Bank's International Centre for the Settlement of Investment Disputes (ICSID), the Stockholm Chamber of Commerce (SCC), or arbitration without any supervising institution, for example pursuant to the rules of the United Nations Commission on International Trade Law (UNCITRAL).[7]

The rapid expansion of the global network of investment protection treaties was linked to the desire of developing countries to attract foreign capital, as well as the inadequacy of traditional international law mechanisms for controlling political risk through diplomatic espousal. While the first BITs were concluded between developing and capital-exporting countries, today developing and transition-economy countries frequently enter into BITs between themselves. Multilateral treaties, such as the ECT, bind a variety of countries across the Eurasian landmass to observe obligations similar to those found in BITs.

Each investment treaty contains its own definition of 'investor' and 'investment', and a description of the actions that may not be taken by the host state in relation to foreign investors and their investments. Nearly all contain a prohibition on expropriation without adequate compensation, covering not only direct seizure or nationalisation, but also indirect or 'creeping' expropriation that destroys investment value or has an effect on ownership rights through regulations or other means.[8] These treaties also normally require that host states accord 'fair and equitable treatment' to qualifying investors and investments, and to refrain from taking actions that would undermine the reasonable expectations that formed the basis for the decision to invest.[9] Another common clause provides for 'full protection

6 The first BIT with a 'direct' arbitration clause benefiting private investors was signed in 1969 between France and Tunisia.

7 The Russian Federation is not a signatory of the 1965 Washington Convention, which forms the legal framework for arbitration at ICSID. As a result, most Russian investment treaties provide only SCC and ad hoc (including UNCITRAL) arbitration options.

8 *Metalclad v United Mexican States*, ICSID Case No ARB(AF)/97/1 (awarding US$16.7 million to a US corporation under the North American Free Trade Agreement as compensation for Mexico's actions in relation to a waste disposal facility, which substantially affected the value of the investment).

9 *CMS v Argentina*, ICSID Case No ARB/01/8 (awarding over US$130 million in compensation to a US corporation under the US-Argentina BIT as compensation for Argentina's dismantling of a regulatory regime that ensured gas transport companies a tariff level providing a reasonable rate of return).

and security' of investments[10] Finally, clauses establishing a right to both national treatment and most-favoured-nation (MFN) treatment prevent host states from discriminating against foreign investors on the basis of their nationality, either in favour of local businesses or in favour of investors from third countries.[11]

BITs and their multilateral cousins, such as the North American Free Trade Agreement and the ECT, have become essential elements of investment planning and management in many parts of the world. The Argentine financial crisis of 2000–2002 gave rise to more than 30 international arbitration cases pursuant to BITs, in which foreign companies claimed that Argentina's response to the challenges of that time destroyed the regulatory regime that had formed the basis of their decision to invest there in the first place. Several of these claims have already been adjudicated, resulting in damages awards in the hundreds of millions of dollars. Why then has there been relatively little attention to investment protection instruments in the context of the Russian Federation, until the Yukos claims brought them to the attention of the world? With Russia pursuing a new nationalist economic policy, particularly in relation to energy resources, why have relatively few foreign investors sought remedies through international investment arbitration?

The answer is rather complex, and relates in part to the Russian Federation's investment treaty programme and the agreements it has signed. This article will provide an overview of international investment protection instruments, review some of the recent cases involving the Russian Government and try to draw some conclusions about the potential of these treaties as tools for the promotion of economic and legal stability in the former Soviet space.

Russia's investment treaty programme

The Soviet Union concluded its first BIT – with its northern neighbour, Finland – in 1989. As perestroika deepened, the Soviet Government concluded several other bilateral treaties with OECD countries, including France, Germany and Canada. Many of these early Soviet BITs were rather conservative in their grant of investor protections – hardly a surprising

10 *Asian Agricultural Products Ltd v Sri Lanka*, ICSID Case No ARB/87/3 (awarding US$460,000 to a UK company under the UK-Sri Lanka BIT as compensation for Sri Lanka's failure to protect a shrimp farm from local military units in search of Tamil rebels).

11 *Marvin Roy Feldman Karpa v United Mexican States*, ICSID Case No ARB(AF)/99/1 (awarding 10 million Mexican pesos to a US national under the North American Free Trade Agreement as compensation for Mexico's failure to provide import tax rebates similar to those offered to Mexican businesses).

circumstance, given the novelty of foreign investment in the slowly liberalising economy.

Most significantly, most of the Soviet BITs (like those concluded by other Socialist countries at the time) include an arbitration clause of limited scope, providing consent to resolve only disputes related to the 'amount or mode of payment of compensation for expropriation'. As a result, there was no possibility to arbitrate claims of discrimination, unfair treatment or other measures that were not serious enough in their impact to constitute expropriation. Indeed, such narrow dispute resolution clauses could be viewed as preventing the arbitration even of disputes about whether expropriation had occurred. According to the position taken by the Russian Federation later in the course of litigation, such disputes had to be submitted to Russian courts in the first instance, and only once such a court confirmed that expropriation had occurred (a highly unlikely outcome by any objective assessment) could an international tribunal accept jurisdiction to assess the compensation due under the applicable investment treaty.

After the Soviet Union disintegrated at the end of 1991, Russia urgently sought to attract foreign capital to support its economic restructuring and recovery. Boris Yeltsin's Government quickly adopted a new model BIT in 1992.[12] This template offered significant improvements vis-à-vis the Soviet model, and in particular provided qualifying investors with the right to arbitrate all disputes arising out of their investments and the rights granted under the treaty. As part of this same liberalisation process, Russia applied for accession to the World Trade Organization (WTO) in 1993.[13] In 1995, Russia signed the ECT, which provided protections equivalent to those found in BITs to investors in the energy sector from all over the Eurasian landmass. By the time Vladimir Putin became President at the beginning of 2000, Russia had signed at least 45 BITs.[14]

The beginning of Putin's administration marked a cardinal change in Russian policy with respect to investment protection treaties. Most importantly, the rate at which new BITs were signed dropped sharply. Only three treaties with relatively insignificant trading partners – Jordan, Thailand and Armenia – were concluded after 1999. Just as disturbing, hardly any investment treaties were ratified by the Duma, an essential prerequisite for any such instrument entering into force. The failure to ratify was particularly

12 The first Russian Federation Model BIT was approved by the Resolution of the Government of Russian Federation on 11 June 1992.

13 Also in 1993, the WTO established the Working Party on Russian accession WTO, available at **www.wto.org/english/thewto_e/acc_e/a1_russie_e.htm**.

14 See **http://icsid.worldbank.org/ICSID/FrontServlet**. This data is based on information provided to ICSID by governments, and may not be exhaustive.

pronounced with respect to treaties representing potentially significant inward capital flows: the US-Russian Federation BIT, for example, was signed in 1994 and has languished in Duma committees ever since. Likewise, the ECT (as noted above, signed in 1995) was never even submitted to the Duma for ratification.

Moreover, the Russian Federation substantially changed the treaty text to which it was prepared to accede. A new Model BIT was adopted by the government in 2001, with a range of important differences from the Yeltsin-era version.[15] In particular, some of the most fundamental substantive protections were excised from the 2001 model, including national treatment, MFN treatment and fair and equitable treatment.[16] A subsequent legislative act appears to have reinserted some of these protections,[17] but the Russian Federation-Armenia BIT of 2001 (as noted, one of only three treaties signed in the 2000s) followed the more limited model precisely.[18] Another significant aspect of the 2001 Model BIT can be found in its dispute resolution provisions. In accordance with Article 7(2), the 2001 model suggests that claims will be subject to arbitration only if all parties agree to this after the dispute arises – an unlikely outcome indeed.

Naturally, not all of Russia's treaties have been drafted in accordance with its model. As is the case with most such agreements, the text reflects a negotiation process and often results in a hybrid. But even where the 2001 model has not been applied, troubling limitations were nevertheless introduced. For example, the Russian Federation-Thailand BIT of 2002 limits the scope of protection to investments that have received specific government approvals in accordance with local law.[19] Such a requirement has been applied strictly by some arbitral tribunals, raising the possibility that

15 Decree No 456 of the Government of the RF of 9 June 2001 'O tipovom soglashenii mezhdu pravitel'stvom RF i pravitel'stvami inostrannykh gosudarstv o pooshchrenii i vzaimnoj zaschite kapitalovlozhenij'. Some treaties had already begun to incorporate provisions similar to the Soviet model. See Lithuania-Russian Federation BIT (1999), Article 10 (dispute resolution clause covering disputes related to investments, 'including' those concerning the mode or amount of compensation for expropriation).

16 Mark Luz, 'New Model Bilateral Investment Treaty: A Step Backwards for Foreign Investors' in *Russian/East European Business & Finance Report*, 15 October 2001.

17 Decree No 229 of the Government of the RF of 11 April 2002 'O vnesenii dopolnenij i izmenenij v tipovoe soglashenie mezhdu pravitel'stvom RF i pravitel'stvami inostrannykh gosudarstv o pooshchrenii i vzaimnoj zaschite kapitalovlozhenij'.

18 Russian Federation-Armenia BIT (2001), Article 2 (no fair and equitable treatment, most-favoured-nation treatment or national treatment provided).

19 Russia-Thailand BIT (2002), Article 2(3).

formal defects in the approval documentation of an investment project could be invoked to prevent redress against later government interference.[20]

The Russian Federation was quick to justify the changes to its BIT practice. Somewhat strangely, certain government officials insisted that the shift in policy was largely due to Russia's likely accession to the WTO,[21] suggesting that the suspension of the treaty ratification process would somehow limit the Russian Federation's negotiations in relation to the multilateral trade body.[22] Ostensibly, the concern was apparently that any trade advantages granted by Russia to WTO members on entry into the organisation would have to be granted to all of Russia's BIT partners by operation of the standard MFN clauses in investment treaties. This excuse is difficult to accept. Most of the BITs that Russia has ratified are with states already members of the WTO, and therefore Russia's entry into the organisation would add little to the advantages BIT partners could hope to obtain. Furthermore, members of international trade organisations routinely avoid generalising the effects of those arrangements by expressly limiting the effect of the MFN clauses in the investment treaties that they sign.[23]

Rising natural resource prices and the stabilisation of the Russian economy after 2000 would appear to be far more likely motivation for the changes in treaty policy. Russia's Deputy Minister of Economic Development and Trade admitted as much in 2001, stating that the freeze on new BITs was undertaken to avoid granting any 'new privileges' to foreign investors.[24] With no particular need to attract foreign capital, and still relatively limited outward investment on the part of Russian companies, the Government could see no particular benefit to limiting its freedom to act in relation to foreign investors.

Whatever the motivation, the result is that the Russian Federation has placed its investment treaty negotiation and ratification programme in stasis. The seizure of the assets of Yukos did nothing to inspire further movement within the Russian government with respect to investment protection treaties. In particular, the potential exposure of the Russian state to arbitration claims

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20 *Philippe Gruslin v Malaysia*, ICSID Case No ARB/Award of 27 September 2000, para 25.5 (rejecting jurisdiction over investments that did not constitute an 'approved project' in accordance with the Belgium-Malaysia BIT).

21 *Russia likely to join WTO in Q3 2008*, RBC News, 19 December 2007, **www.rbcnews.com/free/20071219125531.shtml**.

22 'U investorov otnimaiut prava', *Vedomosti*, 14 June 2001.

23 See, eg, Belgium-Moldova BIT (2002), Art 3(4) (protection against discrimination 'does not extend to privileges that a Contracting Party' extends to investors of a third state by virtue of its participation in or association with a free trade zone, a customs union, a common market or any other form of regional economic organization').

24 'U investorov otnimaiut prava', *Vedomosti*, 14 June 2001.

under the ECT has relegated the ratification of that convention to permanent doldrums – even if the Russian Government does not appear resolved to repudiate it outright.

An early investor victory: *Sedelmayer v Russian Federation*

The caution with which Russia has approached investment treaties and their ratification has not prevented some disgruntled investors from taking their grievances against the government to arbitration. In the wake of the Russian Government bond default of 1998, at least one major investment bank initiated an expropriation claim against the Russian Federation pursuant to the United Kingdom-Russian Federation BIT, conducted under the UNCITRAL arbitration rules. This claim was settled before any decision was rendered by the tribunal.

The first modern investment treaty arbitration to arrive at a verdict against Russia was *Sedelmayer v Russian Federation*.[25] The claimant was Mr Franz Sedelmayer, a German citizen and the sole owner of a business dedicated to the training and equipment of police and security personnel. In 1991, Sedelmayer's company entered into a joint venture with the Leningrad police department. As part of its contribution to the initial capital of the enterprise, the local police provided the use of buildings in a prestigious and peaceful section of the city. The enterprise began to work, but in late 1994 President Yeltsin ordered the joint venture's premises to be repossessed by the government.[26] Mr Sedelmayer was forced to abandon the facilities and leave St Petersburg on short notice, leaving vehicles and other personal effects behind.

In January 1995, Mr Sedelmayer submitted a claim to ad hoc arbitration in Stockholm under the Germany-Russian Federation BIT of 1989. The German treaty was drafted in accordance with the Soviet model, with its characteristically narrow dispute resolution clause. However, it also included an additional Protocol, expanding the scope of arbitral jurisdiction to include disputes arising out of government interference that significantly reduced the value of investments.[27] As a result, Sedelmayer faced no strong

25 *Franz Sedelmayer v Russian Federation*, ad hoc Award of 7 July 1998.

26 Sedelmayer's land and buildings on St Petersburg's prestigious Kammenyj Ostrov were eventually converted into a guest residence for visiting foreign dignitaries, and continues to serve this purpose today.

27 Germany-Russian Federation BIT (1989), Protocol, Article 3.

jurisdictional challenge from the Russian side.[28] In mid-1998, the tribunal issued an award holding the Russian Federation liable for the seizure of Mr Sedelmayer's property.[29] Russia was ordered to pay US$2.35 million plus interest as compensation for his interest in the premises, personal effects and vehicles. The total amount due quickly mounted to nearly US$10 million.

It soon became clear that the Russian Government was not about to honour the Sedelmayer award voluntarily.[30] Mr Sedelmayer sought out Russian state-owned assets in a number of Western European countries, but faced initial difficulties overcoming local laws on sovereign immunity of assets.[31] After several years, however, Mr Sedelmayer was obtained a court order arresting an apartment complex in Cologne, Germany, owned by the KGB's successor organisation, the FSB. He attached the income streams from the tenants to obtain full payment of the award, including interest.[32]

Current issues in investment arbitration against the Russian Federation

Mr Sedelmayer's quest for neutral, international adjudication of his investment dispute is not unique. As noted earlier, a number of claimants have initiated arbitration against the Russian Federation before and since, although none has yet resulted in a final monetary award. The cyclical pattern of Russia's investment treaty practice over the last two decades has left a wide variety of treaty texts in force today. A few of the treaties in force today are modern and textually harmonised with BITs in other parts of the world – Russia's treaties with Norway, Denmark and Greece offer prominent examples.[33] Most of the treaties concluded with Russia's most important trading partners are less clear in their application, presenting difficult

28 The Russian Federation raised six jurisdictional objections: that (1) Mr Sedelmayer was not an 'investor' within the meaning of the BIT; (2) no 'investments' had been made; (3) no expropriation occurred; (4) *lis pendens* prevented adjudication of the dispute; (5) the Russian Federation was not a proper respondent; and (6) the claimant had not complied with pre-arbitration procedures stipulated in the BIT. *Sedelmayer*, at 48. All of these defences were rejected.

29 *Sedelmayer*, at 72–73.

30 Commentators believe that up to 90 per cent of international arbitration awards are satisfied voluntarily, without any need for court intervention or seizure of assets. While the statistics may be somewhat less favourable with respect to awards rendered under bilateral and multilateral investment treaties, voluntary compliance is still relatively common in such cases.

31 'Jilted Yukos shareholders turn to Energy Charter Treaty arbitration', *Investment Treaty News*, 18 November 2004.

32 David Crawford, '*Businessman v Kremlin*: War of Attrition', *Wall Street Journal*, 6 March 2006.

33 Norway-Russian Federation BIT (1995); Denmark-Russian Federation BIT (1993); Greece-Russian Federation BIT (1993).

interpretative questions for many arbitral tribunals faced with treaty claims against the Russian Federation.

In particular, two issues that have arisen in investment treaty practice are relevant in the context of Russia-related disputes: the expansion of arbitration through MFN clauses and the provisional application of unratified treaties – especially the ECT. The eventual resolution of these two thorny problems in future arbitral decisions may pave the way for more reliable dispute settlement against the Russian Federation.

As noted above, nearly all modern BITs include a provision guaranteeing qualified investors MFN treatment. Other than some of the most recent examples (none of which has been ratified), Russian treaties are no exception. In accordance with such clauses, the host state is obligated to accord to investors of the other treaty party treatment no less favourable than that received by investors from third countries. In other words, based on an 'MFN' clause, a qualifying investor can benefit from any rights enjoyed by third-country investors – including rights conferred in another treaty.

The variation in Russian BIT arbitration clauses has been described above. While many Russian treaties (particularly those signed in the Soviet period) include arbitration clauses limited in scope to the amount and mode of payment of compensation for expropriation, others provide for expansive arbitral jurisdiction. This situation raises the question whether an investor from the United Kingdom, who may not arbitrate disputes related to alleged expropriation or breaches of the 'fair and equitable treatment' standard, is treated less favourably than a Norwegian investor, who benefits from a treaty that allows him to do so.

Investment arbitration tribunals have failed to reach any clear decision about whether an MFN clause can be used to rectify this type of 'discrimination', importing more favourable dispute resolution provisions from other treaties signed by the host state. The tribunal in the *Maffezini v Spain* case concluded that the MFN clause covers procedural rights conferred by BIT dispute resolution provisions.[34] But another tribunal, in *Plama v Bulgaria*, ruled that arbitration clauses may only be expanded in this way if the MFN clause in question expressly provides for it (which is almost never the case).[35] Subsequent decisions have been divided, with proponents of both the more restrictive[36] and more expansive interpretation of MFN treatment.[37]

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34 *Emilio Augustin Maffezini v Spain*, ICSID Case No ARB/97/7.

35 *Plama Consortium Ltd v Bulgaria*, ICSID Case No ARB/03/24.

36 *Siemens AG v Argentina*, ICSID Case No ARB/02/8; *Gas Natural SDG SA v Argentina*, ICSID Case No ARB/03/10.

37 *Salini Construttori SpA & Italstrade SpA v Jordan*, ICSID Case No ARB/02/13; *Telenor Mobile Communications SA v Hungary*, ICSID Case No ARB/04/15.

Two recent cases dealing with this issue involved the Russian Federation. In *Berschader v Russian Federation*, two Belgian investors won a public tender for the construction of a new Russian Supreme Court building in Moscow.[38] In September 2001, after work was nearly complete, Putin's office annulled the construction contract, and Ministry of Internal Affairs troops ejected Berschader's personnel from the project site. Millions of dollars remained unpaid for work already done. In August 2004, the Berschaders filed a claim against Russia at the Stockholm Chamber of Commerce under the 1989 Belgium-USSR BIT, claiming compensation of US$13.3 million. The arbitration clause of the treaty established jurisdiction only with respect to disputes 'concerning the amount or mode of compensation to be paid under Article 5 [on expropriation] of the present Treaty'.[39] The Berschader tribunal first concluded that this clause could only be invoked after a Russian court had issued a decision confirming the occurrence of expropriation.[40] Next, the tribunal reviewed the claimants' argument that the expansive dispute resolution clause of the Norway-Russian Federation BIT should apply instead, by operation of the MFN clause. While in principle the arbitrators agreed that MFN treatment could extend to procedural rights, they found that the particular terms of the Belgian treaty were insufficiently clear to allow the importation of the Norwegian arbitration clause. 'An MFN provision in a BIT will only incorporate by reference an arbitration clause from another BIT where the terms of the original BIT clearly and unambiguously so provide or where it can otherwise be clearly inferred that this was the intention of the Contracting Parties.'[41] The tribunal rejected the Berschaders' claims for want of jurisdiction.

The picture was further muddied for potential claimants against the Russian Federation by the late 2007 jurisdictional decision in *RosInvestCo UK v Russian Federation*. RosInvest was the owner of US$7 million in ordinary shares of Yukos. After the Russian Government charged Yukos with tax evasion in December 2004, RosInvest's Yukos shares lost nearly all of their value. In October 2005, the company submitted a claim to arbitration at the Stockholm Chamber of Commerce, pursuant to the United Kingdom-Russian Federation BIT. This treaty included an arbitration clause almost identical to the one at issue in Berschader, as well as a similar MFN clause. Like the Berschader tribunal, the arbitrators in RosInvestCo held that the expropriation claim could not be adjudicated directly under the UK

38 *Vladimir & Moise Berschader v Russian Federation*, SCC Case No V(080/2004), Award of 21 April 2006.

39 Belgium-Russian Federation BIT (1989), Article 10(1).

40 *Berschader*, at para 155.

41 *Berschader*, para 181.

treaty.[42] However, the claimant also argued that the broad dispute resolution provisions of the Denmark-Russian Federation BIT should apply by virtue of the MFN clause. The tribunal focused on the wording of the treaty's MFN clause, which granted to UK investors all superior third-party rights related to the 'management, maintenance, use, enjoyment or disposal of their investments'. The arbitrators reasoned that the right to arbitrate investment disputes must be considered part of the 'use' and 'enjoyment' of the investments in dispute. The tribunal therefore accepted jurisdiction over the claim of expropriation, as provided in the Denmark-Russian Federation BIT.[43]

A second fundamental interpretative question has arisen out of the Russian Federation's decision to stall or cancel the ratification process for a large number of investment protection treaties. There is relatively little debate about the general effect of treaties that have been signed but not ratified. The Vienna Convention on the Law of Treaties, which codifies the most fundamental rules of treaty interpretation and application according to customary international law, specifically provides that signatories must not take actions that would undermine the purpose of a treaty, pending ratification.[44] The corollary of this rule is that the obligations of a treaty do not take full effect until the treaty is ratified in accordance with the signatory state's internal constitutional requirements. The obligations in the interim are 'soft', exhortative and without any effective means of enforcement.

While this general rule may apply to the many BITs that the Russian Federation has signed but never ratified, the situation could be different with respect to the ECT.[45] This is because the ECT contains its own specific provision dealing with the treaty's effect between signature and ratification. Article 45(1) of the ECT states that '[e]ach signatory agrees to apply this Treaty provisionally pending its entry into force ... to the extent that such provisional application is not inconsistent with its constitution, laws or regulations'.[46] The effect that this 'provisional application clause' should

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42 *RosInvest Co Ltd v Russian Federation*, SCC Case No V(079/2005), Decision on Jurisdiction of October 2007, at para 123.

43 *RosInvestCo*, at para 130. A similar result was reached in the recent UNCITRAL arbitration in *European Media Ventures, SA v Czech Republic*, Decision on Jurisdiction of 15 May 2007. The facts of the case were described in English High Court decision that resulted from the respondent's attempt to set aside the award. *Czech Republic v European Media Ventures, SA*, High Court decision of October 2007, para 130.

44 Vienna Convention on the Law of Treaties (1969), Article 18.

45 Ulrich Klaus, 'Gate to Arbitration: The Yukos Case and the Provisional Application of the Energy Charter Treaty to the Russian Federation' (2005) 2(3) *Transnational Dispute Management* .

46 Energy Charter Treaty, Art 45(1), untreaty.un.org/unts/144078_158780/10/8/3517.pdf.

have on the Russian Federation's ECT obligations has yet to be determined directly by an arbitral tribunal. On the one hand, if Article 45(1) is to have any effect at all, one would expect that it would impose greater obligations on the signatory state than the 'soft law' rule of customary international law. Otherwise, why include such an unusual provision in the ECT? On the other hand, it is difficult to imagine that Article 45(1) requires the application of the treaty in full, as if it were already ratified. Such an approach would seem to make ratification by parliamentary vote superfluous, raising a serious concern of 'democratic deficit' and subversion of national constitution structures.

The tribunal in *Petrobart v Kyrgyzstan* dealt with this difficult question in passing.[47] The claimant in the case was a company created under the laws of Gibraltar, which initiated SCC arbitration against Kyrgyzstan under the ECT in relation to gas supplies in Central Asia. When the United Kingdom signed the ECT, it expressly included Gibraltar as one of the territories to which the treaty would apply (along with the Channel Islands and other British offshore possessions). However, when the UK ratified the ECT some months later, the ratification instrument did not include Gibraltar as a covered territory. As a result, Petrobart was a qualifying UK 'investor' only if the United Kingdom's signature gave effect to the ECT, rather than its ratification. The tribunal held that Article 45(1) of the ECT meant that the signature document, with its reference to Gibraltar, was already sufficient for the treaty to enter into effect with respect to the United Kingdom, and that this accession remained in force indefinitely.[48]

The implication of the *Petrobart* decision is that the Russian Federation will be subject to investment arbitration under the ECT even though it has not ratified it. The Plama tribunal seemed to have no difficulty with that concept either, declaring in passing (and without any particular need to do so) that 'Article 45(1) ECT provides that each signatory agrees to apply the treaty provisionally pending its entry into force for such signatory … it follows that Article 26 [on arbitration] provisionally applied from the date of a state's signature …'.[49] A similar conclusion was reached in the *Kardasspoulos v Georgia* arbitration, where expropriatory acts had allegedly occurred between the signing and entry into force of the ECT for Georgia and Greece.[50] The

47 *Petrobart v Kyrgyzstan*, SCC Case No V(126/2003), Award of 29 March 2005.

48 For a critique of the *Petrobart* tribunal's reasoning, see Georgios Petrochilos and Noah Rubins, 'Observations on Petrobart v Kyrgyzstan' (2005) 3 *Stockholm International Arbitration Review* 100.

49 *Plama v Bulgaria*, at para 140.

50 *Kardassopoulos v Georgia*, ICSID Case No ARB/05/18, Decision on Jurisdiction of 6 July 2007. The provisional application of the ECT in this case was not entirely necessary to the upholding of jurisdiction, since the claimants had initiated arbitration under two treaties: the ECT and the Greece-Georgia BIT.

debate continues unabated, however, with the issue of provisional application scheduled to be decided soon in relation to the Yukos-related arbitrations. In particular, a central question will be whether provisional application of the ECT as a whole would be contrary to Russian law, blocking the application of Article 45 according to its terms.[51]

Conclusion

Time will tell whether these and other controversial legal issues will be resolved in favour of claimant investors or the Russian Government. It is already certain that the arbitration claims submitted by Menatep and the other Yukos shareholders will prevent the ratification by the Russian Duma of the ECT (as well as a dozen or so BITs) in the foreseeable future.

It is very unlikely that even total victory in arbitration against the Russian Federation will not lead directly to monetary compensation for aggrieved investors. The enforcement of arbitral awards in Russia has long presented serious problems for foreign contracting parties. The Russian courts' consistent application of international conventions on the enforcement of foreign commercial arbitration awards does appear to be improving in recent years.[52] However, there is little sign that the Russian Government has changed its recalcitrance with respect to arbitration awards rendered against it. The Russian Government has often taken advantage of the inability of foreign creditors to enforce against state assets in Russia, combined with sovereign immunity rules in other countries, to delay payment of awards for years. Only dogged persistence and skilled investigators and lawyers have managed to locate and attach Russian Government assets abroad – as in the Sedelmayer case, described above. In other instances, payment may be even longer in coming.[53]

Nevertheless, the existing Russian investment treaty regime may provide a realistic avenue to limit or rectify unfair and unexpected government

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51 For further discussion, see Andrew Hutcheon and James Spencer, 'Provisional Application of the Energy Charter Treaty' [2008] *The European and Middle Eastern Arbitration Review* 25.

52 Kaj Hober, *Enforcing Foreign Arbitral Awards against Russian Entities* (1999); Vladimir Khvalei, 'Recognition and Enforcement of Foreign Arbitral Awards in the Russian Federation' (2005) 1 *Stockholm International Arbitration Review.*

53 'Noga Takes the Final Step', *Kommersant*, 15 January 2008 (more than a decade after receiving a US$800 million SCC arbitration award against the Russian Federation, the Swiss company Noga continued to search for and attach Russian sovereign assets, battling European sovereign immunity rules all the way); 'Noga Takes Off', *Kommersant*, 18 January 2008 (Noga succeeded in freezing hundreds of millions of dollars in EADS stock held by a Russian state-owned bank, and appeared finally to be near the end of its saga).

interference in commercial affairs. Russia has signed and ratified more than 30 BITs, of which at least half were drafted according to a more or less standard OECD template. Already, many foreign investors in Russia are structuring their investments not only to minimise tax burdens and to access advantageous regulatory regimes, but also to benefit from investment treaty protection. Carefully examining the provisions of investment treaties in force and considering incorporation of project vehicles in appropriate jurisdictions have become an essential part of business planning.

For now, the Russian Federation has been relatively immune from the effects of the investment protection treaties it has signed. But increasing knowledge about the function of these instruments among the foreign investment community has already led to an increasing number of arbitration claims against the government. It is still unclear whether most of these claims will result in enforceable judgments, or influence Russia's policy towards foreign capital. At the very least, these new actions may provide a new way to procure a seat at the negotiating table with a government otherwise disinclined to compromise.