Arbitration Watch:

1. Ukraine prevails as arbitration tribunal splits over lawsuit by publisher,
   By Luke Eric Peterson

   An ICSID tribunal, by a 2-to-1 margin, has found in favour of the Government of
   Ukraine in an investment treaty arbitration brought by the Lithuanian owner of a
   Ukrainian publishing company.

   Tokios Tokeles had accused the Government of then President Leonid Kuchma of
   political harassment of its Ukrainian publishing company, Taki Spravy, following the
publication of political opposition campaign materials, as well as a book about then opposition politician Yulia Tymoshenko.

In 2002, Tokios Tokeles initiated arbitration proceedings at the ICSID facility, alleging various breaches by Ukraine of the Lithuania-Ukraine bilateral investment treaty.

However, in a ruling dated July 26, 2007, the ICSID tribunal hearing the arbitration clam has ruled by a 2-to-1 margin that Ukraine was not in violation of its investment treaty obligations.

Daniel Price, the party-appointed arbitrator for the claimant, in a dissenting opinion, held that the Ukraine Government had violated the terms of Article 3 of the Ukraine-Lithuania BIT by virtue of failing to treat Tokios Tokeles’ investments in a “fair and equitable” manner. (Mr Price, at the time of his appointment, was the head of the law firm Sidley Austin’s trade and dispute resolution practice; earlier this year he was appointed by President George W. Bush as Deputy National Security Advisor for International Economic Affairs).

Meanwhile, a majority opinion authored tribunal president Lord Michael Mustill, and Piero Bernardini, a law professor at the University of Rome, and the Ukraine’s party-appointed arbitrator, held that Ukraine had not violated any of the provisions of the relevant treaty.

The award, as yet, remains unpublished. However, ITN understands that the Ukrainian Government has already signaled its willingness to have the award published by the ICSID facility. Under ICSID rules, either party may release an award unilaterally, but the ICSID may publish an award only with the consent of both parties.

Tokios Tokeles has 120 days in which to seek annulment of the award should it wish to challenge the majority’s ruling.

A press statement released by Ukraine’s co-counsel, the Ukrainian law firms Grischenko & Partners and Proxen & Partners, observes that the Tokios Tokeles arbitration is the second ICSID claim against Ukraine to be resolved on its merits in favour of the Government. An earlier claim by a US investor, Generation Ukraine, was dismissed in 2003 by the ICSID tribunal hearing that case.

The Tokios Tokeles-Ukraine arbitration has not been without controversy. Indeed, the recent split on the merits of the case follows an earlier divided ruling by the tribunal on the question of jurisdiction.

As earlier reported in ITN, then tribunal president French law Professor Prosper Weil resigned his seat on the tribunal after issuing a blistering dissenting jurisdictional opinion which decried the “abuse” of the ICSID system by Ukrainian nationals who sought to arbitrate against their host state by virtue of using a Lithuanian corporate vehicle which –
in the view of the tribunal majority – fell under the protective umbrella of the Lithuania-Ukraine BIT.


2. ICSID has jurisdiction in Energy Charter case against Georgia, as second claim arises, By Luke Eric Peterson

In a decision released last month, an ICSID tribunal has upheld jurisdiction to hear a claim by a Greek national that the Republic of Georgia failed to protect his investments in the gas & oil sector.

Mr. Ioannis Kardassopoulos accuses Georgia of violating the terms of the Energy Charter Treaty, as well as the Greece-Georgia bilateral investment treaty, after issuing a decree which allegedly expropriated a concession which had been earlier granted for reconstruction of energy pipelines and infrastructure.

Georgia had objected to the ICSID tribunal’s jurisdiction over the claim, alleging that the incidents in dispute occurred prior to the entry into force of the two treaties, and raising doubts as to where Mr. Kardassopoulos had any ownership stake in the investments under dispute.

However, in a jurisdictional decision dated July 6, 2007, the presiding tribunal has rejected Georgia’s jurisdictional objections.

In so doing, the tribunal also issued what stands as the first-known ruling to address squarely the question of “provisional application” of the Energy Charter Treaty – an untested legal status which arises under the ECT after a government has signed the treaty, but before that government has moved to ratify the agreement.

TRIBUNAL RULES ON PROVISIONAL APPLICATION OF ENERGY CHARTER

Article 45 of the ECT is relatively unusual amongst international trade and investment treaties in that it provides expressly for provisional application of the treaty pending its entry into force.

Lawyers have long debated what this provision means in concrete terms, with counsel for Mr. Kardassopoulos insisting that Georgia was duty-bound under Article 45 to accord the ECT’s investment protections to Mr. Kardassopoulos following the December 17, 1994 signing of the treaty by Georgia.
For its part, Georgia had countered that it was under no such obligations until April 16, 1998 – the point at which the ECT entered into force on a definitive basis following the ratification of the treaty by 30 states.

The debate would be pivotal insofar as many of the allegations of wrongdoing directed at Georgia by Mr. Kardassopoulos fell in the period between 1994 and 1998 – a time during which Mr. Kardassopoulos alleges that his investments were cancelled and confiscated without compensation.

Ultimately, the tribunal, consisting of Mr. L. Yves Fortier, Prof. Francisco Orrego Vicuna, the party-appointed arbitrator of the claimant, and Sir Arthur Watts, the party-appointed arbitrator of Georgia, would interpret Article 45 so that “each signatory State is obliged, even before the ECT has formally entered into force, to apply the whole ECT as if it had already done so”.

There remained, however, a possibility that provisional application might have been illegal under Greek or Georgian law, which, according to the terms of Article 45, would preclude the treaty from being applied.

Thus, the tribunal would go on to examine both Greek and Georgian law, and reach the conclusion that the law of neither country precluded provisional application of the ECT, thus paving the way for jurisdiction over Mr. Kardassopoulos’s arbitration claim.

**TRIBUNAL FINDS THAT CLAIMANT HAD AN INVESTMENT IN GEORGIA**

The tribunal would also reject a further jurisdictional objection by Georgia to the effect that Mr. Kardassopoulos did not have an investment which would warrant protection under the ECT and the Greek-Georgia BIT.

First, the Georgian Government had argued that it was unproven that Mr. Kardassopoulos had any ownership stake in the Panamanian company which had been used as the vehicle for concluding a joint venture agreement in March of 1992 with a Georgian state-owned enterprise.

Second, the Government contended that the joint venture agreement and a subsequent concession agreement had been concluded by Georgian entities which lacked the legal authority to enter into such agreements, thus rendering those agreements void as a matter of Georgian law and therefore ineligible for protection under the treaties in question.

With respect to the former argument, the tribunal would hold that the onus lay on Georgia to prove that Mr. Kardassopoulos did not have an equity stake in the Panamanian company which had entered into a joint-venture with a Georgian state enterprise. The tribunal would go on to hold that sufficient evidence had been tendered by Mr. Kardassopoulos to demonstrate an ownership interest, and that Georgia had failed to present evidence which would prove otherwise.
Meanwhile, in relation to the second argument, Georgia had pointed, in particular, to a provision of the Greece-Georgia BIT which expressly stipulates that its protections are reserved for those investments which have been made in a manner consistent with the host state’s legislation. Simply put, Georgia argued that the investments were illegal as a matter of Georgian law, and that Mr. Kardassopoulos could not, therefore, invoke international treaty protections to protect such illegal investments.

The tribunal conceded that a literal reading of the Greece-Georgia BIT appeared to exclude investments which were inconsistent with Georgia’s laws, however, the tribunal went on to hold that the object and the purpose of the BIT ought to be considered in this context: namely, to provide broad protection for foreign investment. While the tribunal was of the view that investors could not act illegally in making investments, it took the view that a host state could not elude jurisdiction by virtue of its own failures to comply with its domestic law.

Indeed, the tribunal would go on to concede that the relevant joint venture and concession might well have been illegal as a matter of Georgian law, but that this did not absolve Georgia of potential treaty liability for the protection of those investments.

In the circumstance, the tribunal held that the claimant had received many assurances from senior Georgian officials which served to create a legitimate expectation that the investment “was, indeed, made in accordance with Georgian law and, in the event of breach, would be entitled to treaty protection.”

SECOND INVESTOR FILES RELATED CLAIM AT ICSID

In a recent development, Mr. Kardassopoulos’s Israeli business partner, Mr. Ronald Fuchs, has initiated arbitration against Georgia in relation to Mr. Fuchs’ own share in the aforementioned investments.

That claim, which does not fall under the Energy Charter Treaty, but rather a bilateral investment treaty, was registered by ICSID on July 16, 2007 and a tribunal is in the process of being constituted to hear the case.

3. ANALYSIS: Tribunal’s ruling in Georgia case could resonate in Yukos-Russia dispute

The tribunal ruling in the Kardassopoulos-Georgia case is the first to offer a comprehensive interpretation of Article 45 of the Energy Charter Treaty.

The tribunal’s reasoning will doubtless be closely parsed by lawyers acting on either side of a much larger ongoing set of arbitrations under the Energy Charter Treaty: those related to the multi-Billion Dollar claims against Russia by the former majority owners of the Yukos oil company.
As has been earlier noted in ITN, Group Menatep, the majority Yukos shareholder, turned to international arbitration in February of 2005, accusing the Russian Government of having expropriated their stake in Russia’s then-largest energy corporation.*

Notably, however, Russia has never ratified the Energy Charter Treaty, although the Russian Government did sign the agreement in 1994.

A major issue in the Menatep arbitrations, of which there are three parallel claims**, is presumed to be the question whether Article 45 of the Energy Charter Treaty obliged Russia to accord the ECT’s investment protections to the Menatep investors from the moment of Russia’s signature to the ECT.

Indeed, counsel for Group Menatep, Emmanuel Gaillard of the law firm Shearman & Sterling, in public comments in 2005 said:

“Russia signed the treaty in 1994 and has applied it since then. The Russian Federation has repeatedly stated the importance it attaches to the Treaty in the conduct of its energy policy.”

However, it remains for an arbitral tribunal, convened to hear the Menatep claims, to rule on the provisional application question.

The claimants might have some cause for cautious optimism in view of the decision recently rendered in the Kardassopoulos v. Georgia matter – not least because the Chairman in that case, L. Yves Fortier, also sits as Chair of the three-person tribunal which is hearing the Menatep group of claims. (The remaining arbitrators are Daniel Price and Judge Stephen Schwebel).

Time will tell, of course, whether the Menatep tribunal will elect to follow the interpretation taken in the Kardassopoulos case, given the unique facts and circumstances of the Russian case.

Moreover, Russia will presumably argue that provisional application of the ECT is excluded in the Russian context because such application is illegal as a matter of Russian law - an exception provided for under the terms of Article 45 of the ECT.

This much is clear: the answer to such questions may not become apparent any time soon.

Jurisdictional hearings in the Menatep cases are understood to be scheduled for 2008. Moreover, any jurisdictional ruling in the case might not come to public light because the proceedings are being conducted with a high degree of confidentiality pursuant to the UNCITRAL arbitration rules.

Still, it seems likely that the ruling in the Kardassopoulos case – whatever its significance for the Greek businessman on whose behalf it has been rendered – might have even greater significance in the much more high-stakes set of arbitrations currently being
fought behind closed doors between Yukos’ erstwhile owners and the Russian Government.

Should the tribunal in the Menatep cases find jurisdiction to hear the claims, it would set the stage for a potentially-lengthy set of arguments as to whether Russia is liable for breach of the Energy Charter Treaty in its treatment of Menatep – and whether the tens of Billions of Dollars in compensation sought by the claimants ought to be forthcoming.


** Yukos Universal Ltd. v. Russian Federation; Hulley Enterprises Ltd. v. Russian Federation; and Veteran Petroleum Ltd. v. Russian Federation

4. ICSID tribunal rejects claims of treaty breach by Ecuador in US power case, By Fernando Cabrera Diaz

An arbitration tribunal at the International Centre for Settlement of Investment Disputes (ICSID) has held that Ecuador did not violate the terms of the Ecuador-U.S. Bilateral Investment Treaty (BIT) as had been alleged by a pair of US power companies M.C.I. Power Group, L.C. and New Turbine, Inc. In an award dated July 31, the tribunal dismissed part of the claimants’ case on jurisdiction, and dismissed the remainder on the merits.

The award is the third-known to be rendered on its merits in a BIT arbitration involving Ecuador; as has been reported in ITN, Ecuador earlier prevailed in a claim brought by the Canadian energy firm Encana, but lost another claim brought by US energy company Occidental.*

In particular, the tribunal rejected arguments by MCI and New Turbine that Ecuador had violated the fair and equitable treatment and expropriation provisions of the US-Ecuador BIT.

Notably, the tribunal ruled that portions of the claim fell outside the period when the US-Ecuador treaty was in force, thus limiting the tribunal’s jurisdiction over certain of the claims alleged by the US claimants.

BACKGROUND TO CONTRACTUAL DISPUTE

At the heart of the dispute is a contract signed by Ecuadorian state energy provider INECEL in November of 1995 with Seacoast – a firm owned and controlled by MCI and New Turbine, along with a third party, Old dominion Electric Cooperative
Under the terms of the contract, Seacoast was to install and operate two power plants in Ecuador and sell electricity to INECEL for a period of six months.

However, in early 1996 various differences arose between Seacoast and INECEL, including in relation to the duration of the contract, and performance under the contract.

In April 1996, Seacoast suspended operations, complaining of non-payment of invoices by the state energy provider. Subsequently, in May of 1996 INECEL responded by declaring the contract with Seacoast to be terminated, following the expiration of what it saw as the original 6 month term of the contract.

Seacoast turned to the Ecuadorian courts, seeking some $25 million US from INECEL for damages due to alleged breach of contract. Meanwhile, Seacoast transferred its power generation assets to an Ecuadorian subsidiary owned by MCI, New Turbine and their aforementioned partner ODEC: Power Services Ecuador Ecuapower Cia. Ltda (Ecuapower). At the same time, Seacoast’s accounts receivable were transferred to MCI, New Turbine and ODEC; however Seacoast retained ownership of the legal claim against INECEL.

Later, in December of 1996, MCI and New Turbine sold their interest in Ecuapower to another entity, Anglo Energy Company.

In April of 1997 a first meeting of a so-called Liquidation Commission was held in an effort to resolve differences over the INECEL-Seacoast contract.

However, on February 8, 1999 the Superintendent of Companies (an Ecuadorian government official) revoked Seacoast’s operating permit, citing the fact that the company no longer engages in the original work that the permit had been granted for given that the work had been completed. This led to the termination of the Liquidation Commission, as well as the suspension of negotiations between the parties in the hopes of concluding an arbitration agreement which would provide for the arbitral resolution of the dispute. Moreover, following the suspension of Seacoast’s permit, the Ecuadorian courts ruled that Seacoast’s case against INECEL was rendered null and void.

In response to these developments, the claimants elected to sue Ecuador pursuant to the US-Ecuador BIT.

**ECUADOR RAISES OBJECTIONS TO THE ICSID TRIBUNAL’S JURISDICTION**

For its part, Ecuador raised objections to the tribunal’s jurisdiction, arguing that the BIT, which entered into force on May 11, 1997, could not be applied retroactively. According to Ecuador the two incidents (discussed below) giving rise to the dispute took place before the coming into force of the BIT.

The first incident pointed to by Ecuador was the contract dispute between Seacoast and INECEL that began in early 1996. In September of 1996 Seacoast sued INECEL in
Ecuadorian court for $25 million US claiming that the contract between the two entities had been terminated illegally; that Seacoast was owed money under the contract; and that fines imposed on the company by INECEL were inapplicable.

On Ecuador’s view, the timing of the lawsuit offered proof that the dispute regarding the contract between INECEL and Seacoast had formalized well before the Ecuador-US BIT came into force on May 11, 1997.

Meanwhile, Ecuador pointed to a second incident, which it insisted also fell outside of the US-Ecuador BIT’s remit. Although a power contract was concluded between Ecuapower (a company in which the claimants had a stake) and INECEL in January of 1997, the claimants later transferred their shares in that contract on March 6, 1997 - prior to the entry into force of the Ecuador-US BIT.

Notably, the claimants allege that Ecuadorian officials caused unwarranted delays in the signing of this second contract, which obliged the claimants to sell their investment on unfavourable terms. However, Ecuador countered that the claimants had sold their interests in Ecuapower by the time the US-Ecuador BIT entered into force, and therefore the specific allegations of wrong-doing on the part of Ecuadorian officials were not arbitrable under the US-Ecuador BIT.

The claimants, for their part, insisted that the ICSID tribunal has jurisdiction to examine events that took place before the entry into force of the BIT without violating the principle of non-retroactivity given that the Ecuador’s actions before the treaty could be characterized as “continuing and composite breaches”. What’s more, the claimants argued for a limited retroactivity of the US-Ecuador BIT by arguing that the Most Favoured Nation (MFN) Clause allowed them to seek protection from BITs earlier signed by Ecuador, including the Argentina-Ecuador BIT.

Ultimately, the ICSID tribunal would side with Ecuador on the question of the non-retroactivity of the BIT. In doing so the tribunal also rejected the bid by claimants to invoke the MFN clause in this particular instance so as to benefit from protections contained in BITs earlier concluded by Ecuador.

The tribunal also rejected the claimants’ arguments that Ecuador’s actions were continuing and composite breaches; the tribunal held that it had jurisdiction to hear only allegations of breaches that occurred after the US-Ecuador BIT entered into force.

As a consequence, the substantive breaches plead by the claimants related primarily to alleged bad faith and discrimination by Ecuadorian authorities in the face of the claimants’ efforts to resolve their contractual disputes with Ecuador.

However, on the facts of these claims, the ICSID tribunal would go on to rule that there had been no bad faith or discrimination on the part of Ecuadorian authorities. The tribunal concluded that Ecuador had committed no violations of its substantive legal
obligations under the treaty, including those related to fair and equitable treatment, expropriation and non-arbitrary treatment.

Moreover, the tribunal noted, in summing up its views, that Seacoast had displayed a “certain degree of negligence” by its own failure to pursue domestic avenues which lay open for resolution of certain of the disputes and developments of which it had complained to the ICSID tribunal.

A copy of the MCI v. Ecuador award is available on-line here: http://www.investmentclaims.com/decisions/MCI-Ecuador-Award.pdf


5. Canadian softwood firm must pay all US legal costs associated with NAFTA claim,
By Luke Eric Peterson

A tribunal convened to hear a cluster of NAFTA Chapter 11 arbitrations brought by Canadian lumber firms against the US Government has issued a decision which obliges one of the Canadian firms, Tembec, to cover all of the US Government’s legal costs associated with the defence of that particular claim.

The decision, dated July 19th also brings two other arbitration claims to a close – those brought by Canadian firms Canfor and Terminal – with the costs of those arbitration proceedings to be split between the two firms and the US Government which had jointly agreed to end those proceedings. However, the July 19th decision is most notable for its disposition of the costs associated with the third NAFTA Chapter 11 claim brought by the Canadian company Tembec.

Tembec had balked in 2005 after the US Government successfully moved to have the three pending softwood lumber arbitrations consolidated under the purview of a single tribunal, so that the claims could be heard in a more inexpensive and consistent manner.

Indeed, Tembec turned to the US courts in an effort to overturn the consolidation order, and in the interim the Canadian company dropped its NAFTA Chapter 11 claim. The consolidation tribunal obliged Tembec in January of 2006 when it issued a ruling which terminated the proceedings insofar as they related to Tembec’s arbitration claim. (Canfor and Terminal pressed forward with their own claims, with the tribunal later issuing a
preliminary ruling in 2006 which declined jurisdiction over certain claims, while uphold ing jurisdiction over certain others*)

However, the question of costs associated with Tembec’s case - including arbitrator fees and legal representation costs of the parties - remained outstanding. The consolidation tribunal reserved a ruling on that issue, until such a time as the other consolidated claims (Canfor and Terminal) had been resolved.

SOFTWOOD PACT ENDS ARBITRATIONS AND RAISES ISSUE OF COSTS

Later, in the autumn of 2006 the Governments of Canada and the United States reached an overarching political settlement to the trade disputes which had spawned the various NAFTA Chapter 11 arbitrations (and countless other trade remedy claims) by Canadian lumber firms against the US Government.

In response to the so-called 2006 Softwood Lumber Agreement, Canfor and Terminal moved to withdraw their own NAFTA Chapter 11 arbitration claims against the United States.

Thus, with all three Chapter 11 claims (Canfor, Terminal and Tembec) having been withdrawn, the stage was set for the consolidation tribunal to turn to the question of costs.

Tembec insisted before the tribunal that the costs of its NAFTA Chapter 11 proceeding should be borne by the respective parties. However, the United States argued that Tembec should bear the US Government’s share of the procedural costs as a matter of principle.

In written filings, US Government lawyers argued that “Tembec abandoned its claim on the eve of the jurisdictional hearing”, and should be viewed as the unsuccessful party in the arbitration. The US also expressed a desire that Tembec should shoulder the costs of the proceeding so as to forestall future NAFTA Chapter 11 claimants from engaging in what the US characterized as “abusive tactics”.

TRIBUNAL SAYS COSTS SHALL BE BORNE BY LOSING PARTY

Notably, the consolidation tribunal ruled that it would deviate from the practice seen in some other investment arbitration cases whereby the parties would bear their own legal representation costs and share the costs of the arbitral tribunal. Instead, the tribunal expressed a preference that “costs follow the event”, and that the unsuccessful party in an UNCITRAL proceeding should bear the costs of that proceeding.

The tribunal further determined that Tembec could be characterized as an “unsuccessful party” insofar as the firm had opted unilaterally in 2005 to withdraw its arbitration claim.
The consequence of this ruling was that Tembec was held by the tribunal to owe the United States $271,844.24 (US) for the US Government’s legal representation costs and its share of the arbitrators’ fees.

Notably, Tembec was unsuccessful in persuading the tribunal that it had fallen victim to an eleventh hour “bait and switch” tactic whereby Tembec was allegedly pressured into foregoing what it characterized as a binding legal agreement whereby the two parties would have jointly borne their costs related to the arbitration. For its part, the US Government rejected Tembec’s assertions that there had been any agreement between the two sides to share legal costs, and that Tembec had been pressured into foregoing the benefits of such an agreement.

A copy of the tribunal’s decision is available on the US State Department’s website: http://www.state.gov/documents/organization/90177.pdf


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Briefly Noted:
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6. US investor, S&T Oil Equipment & Machinery, sues Romania over seizure of assets, By Luke Eric Peterson

A US-incorporated firm has had a claim registered at the International Centre for Settlement of Investment Disputes (ICSID), alleging that the Romanian Government has expropriated certain investments without compensation in violation of the US-Romania bilateral investment treaty.

The claim, by S&T Oil Equipment & Machinery was registered by ICSID on July 16, 2007.

In 2003, the US firm bought a majority stake in a newly-privatized Romanian conglomerate, Nitramonia; however S&T alleges that Romanian authorities failed to live up to various commitments made as part of the privatization process. Meanwhile, Romanian authorities accuse S&T of not living up to its own obligations, including in relation to a commitment of several hundred million dollars in working capital.

In 2005, the Romanian Government moved to cancel the privatization agreement with S&T, cancelling the company’s shareholdings, and taking control of its Romanian assets. The Government has since moved to re-privatize the assets by putting them out to tender.
Unverified Romanian news reports have also suggested that a state anti-corruption commission launched an investigation into the sale of the Nitramonia assets to S&T.

The law firm of King & Spalding represents S&T Oil in the ICSID arbitration. Romania is currently tendering for outside legal counsel to represent the Government in this arbitration.

7. Investment Treaty Forum seeks new Senior Research Fellow

The British Institute for International and Comparative Law (BIICL) is seeking a Senior Research Fellow in International Trade and Investment Law. The successful candidate will lead and direct the research program of the BIICL’s Investment Treaty Forum. For more information about the position (whose closing date is August 17, 2007) see:

http://www.biicl.org/opportunities/trade_investment_law/

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