Arbitration Watch:

1. MFN clause used successfully in bid by minority Yukos shareholders to sue Russia, By Luke Eric Peterson

A tribunal has upheld jurisdiction in the first of two known BIT arbitration claims initiated against Russia by minority shareholders of the beleagured Yukos Corporation.

In a Decision on Jurisdiction dated October 2007, but which entered the public domain only recently, an arbitral tribunal has ruled that a UK financial investor,
RosInvest Co UK Ltd, may detour around a restrictive arbitration provision contained in the UK-Soviet Union BIT.

The claimant alleges losses of some $75 million dollars to their shareholdings in the Yukos Corporation as a result of “arbitrary” tax assessments imposed by the Russian Government.

While seemingly protected by the UK-Soviet Union BIT, the claimant faced a formidable barrier to international arbitration in the form of a treaty clause which provides for investor-state arbitration only for a narrow class of disputes.

Indeed, the tribunal consisting of Prof. Karl Heinz Böeckstiegel, Lord Steyn, and Sir Franklin Berman, affirmed that Article 8 of the UK-Soviet BIT precluded an examination of whether the claimants had, in fact, suffered an expropriation. Rather, the treaty only permitted investor-state arbitration in case of disputes over the amount of compensation, or disputes concerning any other matter consequential upon an act of expropriation. In a near-fatal blow for the claimants, the clause did not empower a tribunal to determine whether an expropriation had actually occurred.

In reaching this conclusion, the tribunal echoed a similar finding in another recently-revealed arbitration against Russia, albeit one which was arbitrated under a different bilateral investment treaty.*

Nevertheless, this finding would not prove debilitating to RosInvest’s claim, as the tribunal would go on to find that the MFN clause of the UK-Soviet Union BIT paved the way for the claimants to access a more-generous arbitration clause contained in a BIT between Denmark and Russia.

**MFN CLAUSE USED TO ACCESS ARBITRATION CLAUSE IN ANOTHER BIT**

For its part, Russia protested that Article 3 of the UK-Soviet BIT - which it characterized as a narrow most-favoured nation clause – “could not displace the deliberately chosen narrow grant of jurisdiction in Article 8 with a broad grant of jurisdiction such as the one that Claimant would import from the Denmark-Russia BIT”.

However, the tribunal would reject this Russian position, insisting that the very character and intention of an MFN clause is to ensure that “protection not accepted in one treaty is widened by transferring the protection accorded in another treaty.”

Indeed, the tribunal noted that this effect was generally accepted in relation to substantive treaty protections (for e.g. fair and equitable treatment or full protection and security), and that it could identify no reason not to apply this approach in the procedural context.

In legal terms, the tribunal interpreted Article 3(2) of the BIT – which provides MFN to investors in relation to “their management, maintenance, use, enjoyment or disposal of their investments” – as encompassing access to arbitration in case of expropriation. Thus, if more generous arbitration options were available in other treaties concluded by Russia, Article 3(2) of the UK-Soviet Union BIT permitted an investor to access
those alternatives.

Furthermore, the tribunal noted that the parties to the UK-Soviet Union BIT had specified certain exceptions to the MFN clause, including that it would not entitle investors to lay claim to any more favourable treatment arising out of one party’s membership in a customs union (such as the European Union). However, the tribunal noted that Article 7 of the BIT did not add a further exception to the effect that MFN clauses would not apply to arbitration.

Of particular interest, the tribunal gave short shrift to a string of other cases which have wrestled – often to divergent ends – with MFN clauses in other BIT arbitrations. While enumerating a long list of awards which have explored how MFN clauses apply to the arbitration process, the tribunal noted that there was no need to enter into a detailed discussion of these decisions.

“However, since it is the primary function of this Tribunal to decide the case before it rather than developing further the general discussion on the applicability of MFN clauses to dispute-settlement-provisions, the Tribunal notes that the combined wording in Articles 3 and 7 of the UK-Soviet BIT is not identical to that in any of such other treaties considered in these other decisions. Therefore, they must be interpreted by themselves as was done above and, in the view of this Tribunal, these other decisions do not mandate a change of the interpretation found above.”

Having upheld jurisdiction over RosInvest’s claim, the tribunal now moves to a hearing on the merits as to whether the investor has suffered expropriation without compensation.

For its part, Russia has raised questions as to the timing and expectations of RosInvest’s acquisition of Yukos shares, noting that by the time of RosInvest’s purchase there had been innumerable articles in the international press to the effect that the company was under scrutiny of Russia’s tax authority. Moreover, Russia adds that RosInvest has yet to reveal the price it paid for its shares in Yukos, thus rendering it impossible to assess whether a profit or loss might be realized on those shares.

Meanwhile, on the heels of the jurisdictional ruling in the RosInvest arbitration it will be particularly interesting to see how a separate panel of arbitrators resolves similar issues arising in another Yukos-related claim against the Russian Federation.

That claim, by the Spanish firm, Renta 4 S.V.S.A., was initiated against Russia at the Stockholm Chamber of Commerce in 2007, and alleges breaches of the Spain-Russia BIT. A tribunal consisting of Charles N. Brower, Toby Landau, and Chairperson Jan Paulsson, is presiding in that case.

2. ANALYSIS: RosInvest ruling adds to muddy picture of MFN’s effect on arbitration,
By Luke Eric Peterson

An international arbitration tribunal’s decision to uphold jurisdiction over an investment treaty claim by virtue of the operation of an MFN clause in that treaty is the latest in a string of decisions which have taken sharply divergent views of the application of MFN clauses to arbitration procedures.

Although MFN clauses differ from treaty to treaty, thus providing some pretext for these divergent outcomes, some arbitrators have drafted decisions which might be read as “principled” stands in favour of (or counter to) the use of MFN clauses to open up access to the arbitration provisions of other treaties.

While the tribunal in the RosInvest v. Russia arbitration emphasized its desire to hew to the letter of the UK-Soviet BIT, and declined to discuss the approach taken by other arbitration tribunals, the former tribunal also noted that “it could be argued that, if (MFN) applies to substantive protection, then it should apply even more to ‘only’ procedural protection.”

However, the tribunal added that such an argument was not decisive; instead, the tribunal laid emphasis upon the fact that “an arbitration clause, at least in the context of expropriation, is of the same protective value as any substantive protection afforded by applicable provisions such as Article 5 of the BIT.”

Other tribunals have taken a sharply different view of this question, with a tribunal in the case of Plama v. Bulgaria declining to read an MFN clause – which might cover substantive protections - as covering arbitration matters, unless the treaty left “no doubt” that this was the intention of the parties.

In a subsequent arbitration, Telenor v. Hungary, an ICSID tribunal would reject an attempt by the claimant to invoke the MFN clause so as to access more favourable arbitration options found in other Hungarian treaties. What’s more, that tribunal stressed that it wholeheartedly endorsed what it characterized as the “statement of principle” articulated by the earlier Plama tribunal.

On the other side, a string of tribunals, virtually all in cases involving Argentina, where investors have sought to dispense with lengthy waiting periods found in some Argentine BITs, have taken the contrary view. One such tribunal, in the Gas Natural v. Argentina case, went so far as to state that MFN clauses should be assumed to apply to dispute settlement “as a matter of principle” unless it is clear that the parties intended otherwise.

With tribunals insisting that MFN clauses do or do not apply to dispute settlement as a “matter of principle”, it may be difficult to insist that the sharp difference seen in the cases to date is not evidence of some deeper doctrinal divide on this important question.

While some governments have moved to make explicit whether investment treaty MFN clauses extend to matters of dispute settlement, the preponderance of investment
treaties do not offer any clear guidance on this question. As such, divergent interpretations continue to arise. Indeed, as was reported last month in ITN, another tribunal presiding in a case under the Belgium-Luxembourg BIT with Russia rejected by a 2-to-1 margin a bid by an investor to use an MFN argument similar to that used by RosInvest in its own dispute with Russia.*


3. Ecuador will denounce at least nine bilateral investment treaties,
By Luke Eric Peterson

Amidst growing discontent amongst South American Governments with the system of international investment protection, the Republic of Ecuador has announced plans to withdraw from at least nine bilateral investment treaties.

This latest move by the Ecuadorian Government complements an earlier effort to notify the International Centre for Settlement of Investment Disputes (ICSID) that Ecuador does not wish for certain types of disputes to be subjected to ICSID arbitration. As was reported in ITN last year, Ecuador lodged a notification with ICSID on October 29, 2007 advising the Centre that it will not consent to see disputes over non-renewable resources arbitrated at the Washington-based facility.

On its own, this notification would do little to arrest the initiation of arbitrations against Ecuador at the ICSID. In parallel, the Ecuadorian Government would need to undo the consent to arbitration clauses contained in numerous bilateral investment treaties concluded over the years. These treaties typically offer investors the ability to sue Ecuador under the ICSID system, as well as under other arbitration systems (for e.g. ad-hoc UNCITRAL-based arbitration).

Thus, Ecuador’s latest move appears calculated to begin the process of terminating such treaties.

External Trade Minister Maria Isabel Salvador has signaled that Ecuador plans to denounce treaties with El Salvador, Cuba, Guatemala, Honduras, Nicaragua, the Dominican Republic, Paraguay, Uruguay and Romania. Officially, the Minister says that these treaties have failed to bring noticeable benefits to the Ecuadorian economy. However, whilst in legal force, these treaties might – depending upon their specific wording – provide useful tools for nationals of third countries to incorporate in one of those nine territories prior to making onward investments into Ecuador. Through such a legal maneuver, foreign investors whose own home country lacks a BIT with Ecuador might be able to enjoy BIT protections for their Ecuadorian investments nonetheless. For example, Japanese investors – lacking their own BIT with Ecuador – might incorporate intermediary companies in Paraguay or Uruguay as vehicles for making their investments into Ecuador.

Whilst the Ecuadorian Government is moving to denounce certain of its bilateral investment treaties, the process is not as simple as ‘flicking a switch’. Typically,
investment treaties prescribe that the protections contained therein will continue to apply for a further period after denunciation – usually for pre-existing investments. For example, under the Ecuador-Paraguay treaty, the protections persist for a further 10 years after denunciation.

To date, Ecuador has moved to denounce treaties with a range of developing countries or transition economies. However, the Government is also scrutinizing its other investment treaties, including those with the United States, Canada, and various Western European Governments.

4. UNCITRAL Working Group meets as investor-state questions loom,
By Luke Eric Peterson

A Working Group of the UN Commission on International Trade Law (UNCITRAL) is convening this week in New York City for its latest work-session on revisions to the UNCITRAL rules of arbitration.

As was reported previously in ITN, the International Institute for Sustainable Development (publishers of this newsletter)* and the Center for International Environmental Law have called upon governments to revise the UNCITRAL rules so that investor-state disputes are treated differently than arbitrations between private parties.**

The UNCITRAL rules, while often used to resolve private commercial disputes (for e.g. a contractual falling-out between two businesses), are also commonly included in bilateral investment treaties. In contrast with the rules of the International Centre for Settlement of Investment Disputes (ICSID), the UNCITRAL rules do not provide for any mandatory disclosure of investor-state arbitration proceedings. Moreover, the proceedings themselves tend to be closed to public scrutiny.

An extensive series of interviews with investment treaty arbitration practitioners conducted by Investment Treaty News found that the majority of investment treaty lawsuits initiated in 2006 took place under the less visible UNCITRAL rules, or other commercial arbitration rules.***

It remains to be seen whether UNCITRAL member-governments will move, as part of their ongoing revisions to the UNCITRAL rules, to provide for special rules for arbitrations involving foreign investors and states. ITN will report on the outcome of this week’s Working Group meetings in a subsequent issue.

* Editor's Note: IISD undertakes policy research and analysis and advances policy recommendations in the area of international investment law. Investment Treaty News (ITN) is a reporting service of the IISD with an editorially independent mandate to provide neutral reporting on developments in the area of foreign investment law and policy.

** “NGOs call for transparency as UNCITRAL governments meet in Vienna”, By
A three person panel at the London Court of International Arbitration (LCIA) has rejected an effort by Argentina to disqualify an arbitrator presiding in an investment treaty arbitration brought by the UK-based National Grid company.

Argentina had mounted its challenge to Judd Kessler in July of 2007, following comments voiced by Mr. Kessler at an oral hearing in the case.

Argentina took issue with certain comments by Mr. Kessler, in the course of the proceedings, to the effect that there had been major harm or major change in the expectations of National Grid’s investment. Argentina alleged that these comments raised doubts as to Mr. Kessler’s impartiality to serve as an arbitrator in the case, given that he appeared, in Argentina’s view, to have prejudged certain matters under consideration in the case.

Because the arbitration is proceeding under the UNCITRAL rules of procedure, Argentina invoked Article 10 of these rules, which provide for disqualification of arbitrators “if circumstances exist that give rise to justifiable doubts as to the arbitrator’s impartiality and independence.”

Mr. Kessler declined to step down from the tribunal and offered to the parties a further explanation of his comments, and an offer to include certain corrections in the transcript of the hearing on the merits.

Meanwhile, National Grid rejected Argentina’s challenge and cautioned that it might provide a precedent that would enable any party fearful of losing the case “to analyse every statement of the arbitrators in hope that it proves their impartiality, and, hence, provides a basis for frustrating the arbitration proceedings.”

Ultimately, a three person panel, consisting of Dr. Klaus Sachs, Mr. Paul Hannon, and Dr. Hassan Ali Radhi, conceded that Mr. Kessler’s statement, taken in isolation, might lead a reasonable third person to think that Mr. Kessler “had already taken a firm view on issues which are key to the final result of the arbitration.” However, the panel added that the entire context of Mr. Kessler’s intervention – combined with the fact that it was in Spanish, his second language – served to allay such apprehensions.

The panel also noted that Mr. Kessler had endeavoured to clarify his remarks at the hearing, in particular, by clarifying that these were “allegations” of harm by National Grid. As such, the panel was of the view that Mr. Kessler could not be said to be
“prejudiced”, even if certain of his statements were “unfortunate” when viewed out of their context.

The National Grid proceeding remains ongoing, with an award on the merits likely to materialize sometime in 2008.

A copy of the LCIA decision on the challenge to Mr. Kessler is now available in Investment Treaty News’ on-line documents centre: http://www.iisd.org/investment/itn/documents.asp

6. NAFTA tribunal declines jurisdiction in Canadian cattle ranchers’ dispute with the US, By Damon Vis-Dunbar

A NAFTA tribunal has declined jurisdiction in a dispute that pitted Canadian cattle producers against the U.S. Government. The case was notable in that the Canadian ranchers alleged breaches of NAFTA’s investment chapter, despite the fact that they had not made investments in U.S. territory.

The ranchers launched the claim after a cow in Canada tested positive for Bovine Spongiform Encephalopathy (aka mad cow disease), leading the United States to shut its border with Canada to live cattle between 2003 and 2005. Canada has maintained that its cattle posed no risk to its southern neighbor, and the Canadian ranchers assert that the ban was motivated by economic and political interests.

In a 28 January award, the three-member tribunal was unanimous in the opinion that it does not hold jurisdiction to hear a NAFTA Chapter 11 claim against the United States when the investments are located outside U.S. territory.

At issue was whether NAFTA’s investment chapter was, as the United States asserted, “no more than a BIT dropped into a free trade agreement ....” According to the claimants, the chapter’s ambitions are broader, given that NAFTA’s overarching goal is the free flow of goods, services and investments.

Counsel for the Canadian ranchers argued that while certain provisions in the investment chapter do impose territorial requirements, others do not. These “hybrid provisions”, on the claimants’ interpretation, were meant to protect “investors” regardless of their geographical location.

However, the United States dismissed this reasoning as “absurd”.

“Such an interpretation,” the US State Department argued, “would constitute a radical departure from the obligations that the NAFTA Parties, or any State Party to an international investment agreement, have ever undertaken with respect to foreign investors. It would create an avenue for direct claims against states by foreign nationals for matters that are ... quintessentially trade disputes ....”

(In contrast to NAFTA’s investor-state mechanism for settling investment disputes, NAFTA trade disputes are handled between governments.)
While the tribunal declined jurisdiction over the case, it did not agree with United State’s assertion that NAFTA’s Chapter Eleven is equivalent to a bilateral investment treaty. For one, the NAFTA is a multilateral agreement between three parties: the US, Canada, and Mexico. But more importantly, it interacts with other parts of the NAFTA (for e.g., Chapter 11 is subordinate to other NAFTA chapters).

However, the tribunal conceded that Chapter Eleven was analogous to a BIT in that it offers legal protections only to those investors with foreign investments in another host country.

“The fact that the NAFTA indisputably seeks to promote economic integration among industries in the three States Parties does not mean that the border has been eliminated for purposes of border protection, no matter how similar or integrated the industries on both sides may be,” states the award.

The tribunal notes that the claimant could not point to any other investment provisions in free trade agreements that protected domestic as well as foreign investors.

Ultimately, the tribunal advised that the proper remedy to settle the underlying dispute is the state-state dispute mechanism in NAFTA’s Chapter 20 on General Dispute Settlement; not the investor-state arbitration mechanism in Chapter 11.

“Oh indeed, taking the Claimant’s factual submissions at face value,” the tribunal added, “Claimants would be wholly justified in pressing their government to seek recourse against the U.S. Government for the measures at issue. Although such a remedy may be less attractive to Claimants than a direct claim for damages, it is, in this Tribunal’s view the remedy provided by the NAFTA for a trade dispute of this nature.”

Although the claimants did not prevail in their case, the tribunal ordered that costs for the arbitration should be shared equally between the two parties.

The ruling in the case echoes another ruling in a separate claim brought by a group of US claimants against the Government of Mexico, where the lack of investments in the Mexican territory also proved a bar to arbitration of the claim.*

The Award on Jurisdiction in The Canadian Cattlemen for Fair Trade vs. The United States of America is available online:


7. Poland says talks progressing with Eureko as arbitration damages phase continues, By Luke Eric Peterson

Settlement talks are underway between a Dutch-owned financial institution and the
Polish Government, in an effort to resolve a long-running dispute over the privatization of Poland’s largest insurance company.

Representatives of Eureko and the Polish Treasury confirm that talks are ongoing, with the latest round occurring on January 17th. The two sides characterize the discussions as “constructive” and say that they hope to “find an amicable way” to resolve the dispute.

At the same time, Eureko and Poland acknowledge that an ad-hoc arbitration proceeding remains ongoing, with the tribunal now focused on assessing damages in the dispute.

Eureko turned to arbitration in 2003, alleging that Poland had violated the terms of the Poland-Netherlands bilateral investment treaty. In 2005, a divided tribunal held by a 2-to-1 margin that Poland had breached its treaty obligations.*

At issue in the dispute is a fight for control of Powszechny Zaklad Ubezpieczen S.A. (PZU), which Poland partially-privatized in the late 1990s. Following Eureko’s initial purchase of a minority stake in the , Eureko and Poland quarreled over an alleged commitment by Poland to proceed with a public sale of the remaining shares in PZU.

During this period, public opinion in Poland swung decisively against the sale of the country’s insurance giant to a foreign investor.

A majority of the three-person arbitration tribunal would rule that this “abrupt about-face” adversely affected Eureko’s investments in Poland – which were held to include a “firm commitment” on the part of Poland to proceed with an Initial Public Offering of the remainder of the PZU shares.

The dissenting arbitrator, Prof. Jerzy Rajski, criticized the majority for transforming what should have been a contractual dispute into an internationally justiciable matter. In a sharply-worded dissent, Rajski lamented the majority’s willingness to permit foreign investors to ignore contractually agreed dispute-resolution procedures (in this case, the Polish courts).

However, a challenge to the award filed by Poland in the Belgian courts proved unsuccessful. To date, no appeal of that Belgian court ruling has been filed by Poland.

Poland also mounted a high-stakes challenge to Eureko’s party-appointed arbitrator, Judge Stephen Schwebel. That challenge was ultimately dismissed by the Belgian courts, and affirmed on appeal to a higher court in that country.

Following this recourse to the Belgian courts, the international arbitration proceedings resumed, with the arbitrators now focused upon assessing the damages owing to Eureko. A recent report in the Polish press suggests that Eureko is seeking a massive 10 Billion euros in compensation for the treaty breaches.

* For a full account of the 2005 arbitral ruling, see: “Divided tribunal finds Polish privatization ‘reversal’ violates treaty with Netherlands”, By Luke Eric Peterson,
An international law firm is advising on-line gambling businesses shut out of the US market to invoke protections contained in international investment agreements (IIAs) as an alternative to state-to-state challenges to the ban at the World Trade Organization.

In a recent briefing note, the law firm Herbert Smith suggests that the extensive investment liberalization provisions in some US investment treaties (bilateral investment treaties and free trade agreements) grant foreign on-line gambling services the same access to the US market as enjoyed by domestic gambling businesses.

The briefing note comes as the government of Antigua remains locked in a protracted WTO dispute with the United States after on-line casinos were blocked from accessing gamblers in the US. The US asserts that its domestic laws do not permit cross-border gambling, and that it never intended to grant foreign on-line gambling operations access under the WTO’s General Agreement on Trade in Services (GATS).

However, certain American-owned on-line casinos are permitted to operate in the US, which foreign operators charge is discriminatory and in breach of US commitments under the GATS. The Antiguan government has sought to press the issue by dragging the US before WTO dispute settlement panels.

Thus far, WTO panels have sided with Antigua in the dispute, although this has not brought immediate relief to on-line casino operators based on the island. In December, a WTO panel granted Antigua the right to enact sanctions of up to $21 million against American-held copyrights. Antigua had argued that common forms of cross-retaliation, such as higher tariffs on goods and services, would have damaged the small island state’s economy far more than it would hurt the US.

However, since no country has ever cross-retaliated with WTO-approved action against intellectual property, it is unclear how Antigua would go about enacting the sanctions.

As an alternative to WTO litigation initiated by states, Herbert Smith points out that U.S. investment treaties often include wide-ranging market access provisions, granting foreign investors the right to establish themselves in the US market, albeit with certain restrictions and with sensitive sectors excluded.

“In the event the US denies an investor permission to establish a gaming business, this may well amount to a breach of its treaty obligations. The putative investor could then choose to enforce its rights by recourse to the dispute resolution mechanism contained in the applicable IIA,” says the briefing note.
According to the firm, arbitration under the dispute settlement mechanisms found in IIAs could provide more direct relief to affected investors. In contrast to the state-to-state WTO dispute settlement system, international investment treaties would allow an arbitral tribunal to award damages directly to on-line casino operators, should the US be found in breach of its treaty obligations.

To date, ITN is not aware of any on-line casino businesses that have pursued damages against the US for breach of IIAs.


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**Briefly Noted:**
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9. Investmentclaims.com re-launches under Oxford banner

One of two well-known websites dedicated to collecting and publishing free copies of investment treaty arbitration rulings has entered into a partnership with Oxford University Press.

Investmentclaims.com has re-launched its free website and will offer a premium subscription service starting in March of 2008. For more information visit:

http://www.investmentclaims.com

Another (unrelated) service maintained by Prof. Andrew Newcombe of the University of Victoria offers free access to publicly-available arbitration rulings at this address:

http://ita.law.uvic.ca/

To subscribe to ITN, email the editor: lpeterson@iisd.ca

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