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I. Introduction

Like much of the rest of the world, Russia had a difficult year in 2009. An economy growing at a 7.5% annual pace in the second quarter of 2008 reversed course and was shrinking at an annual rate of 10.9% by the second quarter of 2009. Even now, as the rest of the world appears to be emerging from recession, the steep decline in Russia's GDP continues and the State budget is running a substantial deficit despite a rebound in the price of oil and other natural resources. Some commentators have even suggested that Russia has lost its right to be part of "BRIC" (Brazil, Russia, India, China), the unofficial club of major rapidly developing economies, and suggest shortening the acronym to "BIC." Russia itself seems to have become more cautious about the idea of global economic integration, as illustrated by the recent changes in its WTO accession strategy and its withdrawal from the Energy Charter Treaty.

But none of this means that the economic importance of Russia to the rest of the world is diminishing. Russia's private and state-owned companies continue to expand their operations beyond Russia's borders, even if the rate of this expansion has slowed. With its vast natural resources, well-educated population, and geopolitical influence from Europe to the Middle and Far East, Russia will continue to be a place of interest for many companies, institutions, and individuals.

Russia has been criticized for its policies as well. Some human rights and rule-of-law advocates have complained that Russia remains an autocratic State and that the government has failed to follow through on promises to combat corruption, promote an independent judiciary, and ensure adequate protections for the rights of its own citizens and foreigners (including foreign investors).

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On the positive side, political relations with the West (and with the United States in particular) appear to have improved, despite dire predictions of a new cold war following Russia's military conflict with Georgia in August 2008, over South Ossetia and Abkhasia. Presidents Dmitry Medvedev and Barack Obama, two lawyers of a new generation, appear willing to give each other the benefit of the doubt. The United States abandoned deployment of its missile defense system in Europe, and Russia, in turn, appears genuinely willing to cooperate on a diverse range of matters from nuclear nonproliferation and disarmament to fighting terrorism and international financial crime.

Foreign investment and the rule of law in Russia are the themes connecting the next three sections (II, III, and IV) of this article, which discusses recent legal developments. Section II traces the implementation, interpretation, and application of Russia's April 2008 law on investment in strategic sectors (Strategic Sectors Law),[1] the substantive provisions of which were discussed in last year's edition of the Year in Review.[2] Section III provides an update on the ongoing second trial of Mikhail Khodorkovsky and Platon Lebedev, the principals of YUKOS Oil Company, whose assets were taken over by the Russian State several years ago. Although this trial has received somewhat less publicity in the West than the first one (which resulted in nine-year sentences for the two men), it nevertheless appears certain to have a profound effect on the development of Russian criminal law and on perceptions of the Russian justice system. Finally, Section IV examines one of the latest international investment tribunal decisions involving Russia. The Tribunal's decision in that case—*Renta 4 v. Russian Federation*—finds jurisdiction for claims against Russia based on a new interpretation of standard language contained in Russia's bilateral investment treaties with a number of other nations.

II. FOREIGN INVESTMENT: The Strategic Sectors Law in Practice

A. BACKGROUND OF THE LAW

Signed into law on April 29, 2008, the Strategic Sectors Law regulates foreign investment into forty-two pre-defined industries that generally affect national security and defense.[3] The Law's coverage extends to two main categories—specified acquisitions of Russian companies by foreign investors under Article 7 and the registration of existing foreign ownership of five percent or more of covered enterprises under Article 14.[4] Article 7 applies to specified acquisitions that result in foreign control of Russian enterprises.[5] The Strategic Sectors Law also establishes procedures for registering foreign ownership and obtaining approval for proposed acquisitions and assigns responsibility to different bodies for carrying out this process.[6]

1. Federal'nyi Zakon O Poryadke Osushchestvleniya Inostrannykh Investitsii v Khozyaijstvennye Obshchestva, Imeyushchie Strategichesoe Znachenie dlya Natsional'noi Bezopasnosti Rossiiskoi Federatsii [SZ RF] [Federal Law on the Framework for the Realization of Foreign Investment in Economic Organizations Having a Strategic Significance for the National Security of the Russian Federation], 2008 No. 57-FZ, *available at* http://www.rg.ru/2008/05/07/investicii-fz-dok.html [hereinafter Federal'nyi Zakon].

2. *See* Franklin E. Gill, et al., *Russia and Ukraine*, 43 INT'L LAW. 1173 (2009).

3. Federal'nyi Zakon, art. 6.

4. *Id.* arts. 7, 14.

5. *Id.* art. 7, ¶ 1-5.

6. *Id.* arts. 8-14.

Several regulations and decrees regarding the Strategic Sectors Law have been adopted since the Law's entry into force. In July 2008, the Russian government assigned responsibility for the Law's implementation to the Federal Anti-Monopoly Service (FAS) and the Governmental Commission on Control of Foreign Investment in the Russian Federation (Commission).[7] Shortly thereafter, the FAS established the Administration on the Control of Foreign Investment to handle all Strategic Sectors Law issues.[8] The government also took steps to clarify some of the Law's details, such as creating a list of all critical technologies[9] and publishing model formats of the Law's various applications.[10] Finally, in October 2008, the FAS announced that acquisition of Russian banks by foreign investors would not be covered by the Strategic Sectors Law and thus would not require prior approval.[11]

B. Implementation of the Law

Despite the recent decline of investment in Russia, the FAS and the Commission received a relatively steady flow of applications pursuant to the Strategic Sectors Law. From August 2008 to September 2009, the FAS received 108 requests for clarifications of the Law's provisions, 87 applications from investors seeking preliminary approval for specific deals under Article 7, and 323 notifications under Article 14.[12] Of the eighty-seven applications seeking approval, twenty-three were returned to the applicants based on a finding that the proposed transaction would not result in the applicants obtaining control over the strategic enterprise, and seven were returned without examination due to incomplete ap-

7. Postanovlenie Pravitel'stva Rossiiskoi Federatsii O Pravitel'stvennoi Kommissii po Kontroliu za Osushchestvleniem Inostrannykh Investitsii v Rossiiskoi Federatsii, [SZ RF] [Governmental Commission on Control of Foreign Investment in the Russian Federation] 2008, No. 510, *available at* http://www.fas.gov.ru/law/19644.shtml (last visited Jan. 14, 2010).

8. Press Release, FAS Rossii, V FAS Rossii Sozdano Upravlenie Kontrolya Inostrannykh Investitsii [FAS Russia Established Managed Control of Foreign Investment] (July 10, 2008), *available at* http://fas.gov.ru/news/n_19651.shtml.

9. Rasporyazhenie Pravitel'stva Rossiiskoi Federatsii–Perechen' Tekhnologii, Imeyushchikh Vazhnoe Sotsial'no-Ekonomicheskoe Znachenie ili Vazhnoe Znachenie dlya Oborony Strany i Bezopasnosti Gosudarstva (kriticheskie tekhnologii) [SZ RF] [Administration on the Control of Foreign Investment List of Techonologies that are of Social or Economic Significance for National Defense and Security (critical technologies)], 2008, No. 1243-r, *available at* http://government.ru/content/governmentactivity/rfgovernmentdecisions/archive/2008/08/25/4706538.htm, summary by White & Case, Review Legislation, http://www.whitecase.ru/russian/index.phtml?part=update&u_id=491 (last visited Jan. 31, 2010).

10. Postanovlenie Pravitel'stva RF ot 27.10.2008 [SZ RF] [Approval of Rules] 2008, No. 795, *available at* http://fas.gov.ru/law/strategy/21084.shtml; Prikaz FAS ot 13.08.2008 [Approval of Business Plan] 2008, No. 308, http://www.fas.gov.ru/law/20105.shtml (last visited Nov. 16, 2009); Prikaz FAS ot 17.09.2008 No. 357, http://www.fas.gov.ru/law/20895.shtml; Postanovlenie Pravitel'stva RF ot 17.10.2009 [Preliminary Approval of Transactions] 2009, No. 838, http://www.fas.gov.ru/law/strategy/27597.shtml.

11. *Foreigners Need No Gov't Permission to Buy Russian Banks*, RBC News, Oct. 10, 2008, http://www.rbcnews.com/free/20081010183407.shtml.

12. Svetlana Levchenko, *Praktika Osushchestvleniya Inostrannykh Investitsii v Xozyaistvennye Obshchestva, Imeyushchie Strategicheskoe Znachenie dlya Obespecheniya Oborony Strany I Bezopasnosti Gosudarstva* [Presentation from a Conference of the Association of European Businesses in Russia] Sept. 17, 2009, *available at* http://www.aebrus.ru/application/views/aebrus/files/events_files/M&A_all_presentations_file_2009_09_17_17_01_20.pdf.

plication materials.[13] Approximately twenty were examined by the Commission, which extended the review period for at least nine.[14]

The Commission's first meeting was held on October 10, 2008, and considered only two applications that appeared to be "ideal" test cases. The first was Alenia Aeronautica's acquisition of a twenty-five blocking stake in Sukhoi Civil Aircraft from Sukhoi Aviation for $183.1 million.[15] The acquisition itself was never contentious and was ultimately completed by the two sides without controversy.[16] One problem with considering the Alenia case as a useful test of the Strategic Sectors Law is that then-President Putin had approved the deal before the Strategic Sectors Law entered into force.[17]

The second deal approved at the first Commission meeting was Archangel Diamond Corporation's (ADC) acquisition of a 49.9% stake in Arkhangelskoe Geologodobychnoe Predpriyatie (AGP).[18] ADC, a Canadian subsidiary of the De Beers Company, had been involved in a bitter, decade-long dispute with Lukoil over AGP, which owns exclusive rights to the Verkhotina Grib pipe diamond mine in Arkhangelsk, Russia.[19] The companies came to an informal agreement on the dispute in a meeting mediated by then-President Putin in April 2008, just before the Strategic Sectors Law came into effect.[20] Thus, even though the subsequent contractual arrangement fell within the Law's purview, the agreement was yet another example of a deal that had already received tacit approval at the highest level before the Law's entry into force. It is noteworthy, however, that after the Commission approved the deal at its October meeting, it issued a formal approval with a condition "that diamonds extracted . . . are processed in Russia in volumes to be agreed with the Russian Government."[21] The exact contours of this condition were never agreed to and, in December 2008, ADC issued a Notification of Termination Event, which stated that ADC would exercise its option to terminate the Share Purchase Agreement (SPA) if the issues with the Russian government were not settled by December 31, 2008.[22] The

13. A A.G. Tsyganov & A.N. Levchenko, Zakon No. 57-FZ: Pervye Itogi Primeneniya, Aug. 25, 2009, http://fas.gov.ru/article/a_26123.shtml (last visited Nov. 9, 2009).

14. *Id.*

15. Gleb Stolyarov, *Alenia Priletela*, VEDOMOSTI, Apr. 8, 2009, http://www.vedomosti.ru/newspaper/opinions/2009/04/08/190076 (Russ.).

16. Press Release, Finmeccanica Signs New Agreements in Russian and Further Reinforces its Presence in the Country (Apr. 7, 2009), *available at* http://www.finmeccanica.com/EN/Common/files/Holding/Corporate/Sala_stampa/Comunicati_stampa/Anno_2009/ComFin_AccordoRussia_07_04_09_ING.pdf.

17. *See* AFX News Limited, *Russia's Putin Approves Alenia Buy of 25 pct Stake in Sukhoi*, FORBES, Jan. 14, 2008, http://www.forbes.com/feeds/afx/2008/01/14/afx4526790.html.

18. Anastasiv Savinykh, *Investorov Puskayut Parami*, IZVESTIYA, Oct. 13, 2008, http://www.izvestia.ru/economic/article3121497/index.html (Russ.).

19. John Helmer, *Russian Raiders Bury Hatchet with De Beers over Archangel Diamond–But Who Will Wield the Shovel?*, MINEWEB, Apr. 16, 2008, http://www.mineweb.com/mineweb/view/mineweb/en/page37?oid=51181&sn=Detail.

20. *Id.*

21. Press Release, Archangel Diamond Corp., Archangel Diamond Corporation Receives Formal Decision of Russian Government Conditional Consent for its Acquisition of a 49.99% Interest in AGD (Oct. 29, 2008), *available at* http://www.archangeldiamond.com/pdf/ADC_News-Release-Oct-29-08.pdf.

22. Press Release, Archangel Diamond Corp., Archangel Diamond Corporation Delivers Notification of Termination Event (Dec. 8, 2008), http://www.archangeldiamond.com/pdf/ADC_News-Release-Dec-8-08.pdf.

issues were not resolved, and ADC formally terminated the SPA in January 2009.[23] Finally, in May 2009, De Beers reportedly voted to sell its stake in ADC to "a lawyer-managed US fund, which is well known as an investor in high-value litigations [sic], with a strong record of winning large settlements for the cases it has taken on."[24]

On February 4, 2009, the Commission held its second meeting, this time giving its approval to at least three acquisitions. First, Barrick Gold, a Canadian corporation, was allowed to purchase twenty-nine percent of Fyodorova Tundra from Norwegian state investors, bringing its total stake to seventy-nine percent.[25] Second, Universal Cargo Logistics Holding BV (UCLH) purchased the Taganrog Shipyard from Valars Group.[26] The latter purchasers, though Russian, were forced to comply with the Strategic Sectors Law because they made the purchase through offshore entities.[27] Finally, Ukrainian state-owned OAO "Hartron" purchased additional shares of CJSC "Kosmotras," yielding a total stake of 49.74%.[28]

On June 8, 2009, the Commission held a third and relatively uneventful meeting. The only deal approved was Nafta-Mokva's acquisition of fifteen percent of Polyus Gold from Interros, increasing its total share to thirty-seven percent.[29]

At its fourth meeting, on September 30, 2009, the Commission made decisions on ten applications from a slightly larger pool.[30] Of these ten applications, details on at least five were publicly reported, including: Itera's purchase of twenty-one percent of Signeftgaz's shares from ACRON, bringing its total holdings to forty-nine percent;[31] Polymetall's acquisition of OOO "Mayskoye" from Roman Abramovich's Highland Gold Mining;[32] Universal Cargo Logistics Holding BV's purchase of the Tuapse Seaport from Novolipetsk

23. Press Release, Archangel Diamond Corp., Archangel Diamond Corporation Terminates Transaction for Purchase of Shares in AGD (Jan. 12, 2009), http://www.archangeldiamond.com/pdf/ADC_News-Release-Jan-12-09.pdf.

24. De Beers Sells Archangel Diamond to Litigation Attack Fund, http://johnhelmer.net/?p=1173 (June 1, 2009).

25. Andrei Biryukov & Maksim Tovkailo, *Vladimir Putin Odaril Inostrantsev Zolotom, Platinoi I Palladiem*, GZT.RU NEWS, Feb. 4, 2009, http://www.gzt.ru/business/2009/02/04/223032.html (Russ.).

26. Jesse Heath, *Strategic Industries Law Update*, RUSSIA MONITOR, May 4, 2009, http://www.therussiamonitor.com/2009/05/strategic-industries-law-update.html.

27. Biryukov & Tovkailo, *supra* note 25.

28. *Pravitel'stvennaya Komissiya Odobrila Sdelki po Vkhozhdeniyu Zarubezhnykh Kompanii v Kapital Strategicheskikh Predpriyatii RF*, ROSBUSINESSCONSULTING, Feb. 4, 2009, http://www.rbc.ru/rbcfreenews/20090204225553.shtml.

29. *Kerimov Will Boost Polyus Stake to Thirty-seven Percent*, MOSCOW TIMES, Apr. 20, 2009, http://www.themoscowtimes.com/news/article/376359.html; *Kerimovu Razreshili Kupit' Dolyu v 'Polyus Zoloto'*, STRANA.RU, June 8, 2009, http://www.strana.ru/doc.html?id=129010&cid=423 (Russ.).

30. *Pravkomissiya Rassmotrit Bolee 10 Zayavok Inostrannykh Investorov o Pokupke Aktivov v RF*, IZVESTIYA, Sept. 29, 2009, http://www.izvestia.ru/news/news216834 (Russ.).

31. *Pravitel'stvennaya Komissiya Odobrila Sdelku o Priobretenii 'Iteroi' forty-nine percent Aktsii 'Sibneftegaza,'* ROSBIZNISKONSALTIN, Sept. 30, 2009, http://quote.rbc.ru/stocks/fond/index.shtml?2009/09/30/32573673 (Russ.).

32. *Pravitel'Stvennaya Komissiya Odobrila Sdelku po Pokupke 'Polimetallom' Zolotorudnoi Kompanii 'Mayskoe*, ROSBIZNISKONSALTIN, Sept. 30, 2009, http://spb.rbc.ru/freenews/20090930202801.shtml (Russ.).

Steel;[33] and Transmashholding's acquisition of shares in Tverskoi Mashinostroitel'ny Zavod.[34]

C. Early Impressions

Initial implementations of the Law suggest that it is neither a death knell nor a panacea for foreign investments in Russia. Several applications had been approved by the first anniversary of the Law, and hundreds of filings have been processed without incident. Even in sensitive industries like aircraft production and seaports, acquisitions went through without any political meddling.

At the same time, the case of ADC reveals some truths about Russia's investment climate that raise questions about the Strategic Sectors Law's effectiveness. First, even the combination of an initial approval by then-President Putin followed by formal approval by the Commission, headed by now-Prime Minister Putin, was insufficient to enable ADC to assert its rights as an investor. This suggests that Russia's poor investment climate stems not simply from high-level politics and state intervention but also from poor business practices by local partners and purely local administrative interference. In other words, even though the President or the Prime Minister may officially support more foreign investment, this often has little influence over the reality faced by foreign companies seeking to invest in a particular enterprise. The problems faced by ADC show that Russia's investment environment is plagued by deep cultural issues regarding a lack of respect for property rights and interference with business relations. Therefore, the Strategic Sectors Law is only one small piece of a broader effort that Russia must make to transform its business environment to bring it closer to international norms of transparency and consistency.

III. LAW: The Impact of the Second Trial of Khodorkovsky and Lebedev

The second trial of Mikhail Khodorkovsky and Platon Lebedev progressed slowly in the Khamovnicheski District Court of Moscow. The prosecution completed its five-month-long documentary evidence presentation, and the trial is currently in the stage of the prosecution examining witnesses. After that, the defense will have its turn.

Khodorkovsky and Lebedev are former top managers and shareholders of YUKOS, which was once a major Russian oil company. In 2003, Khodorkovsky and Lebedev were arrested, and in 2005 sentenced to prison terms of eight years on tax evasion and fraud charges related to their managerial activities in YUKOS. Basically, the tax evasion charges were related to their use of a tax-minimization technique that was found abusive: selling oil through YUKOS subsidiaries incorporated in low-tax Russian regions. Related tax claims ultimately led YUKOS itself to bankruptcy in 2006.

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33. *Pravitel'stvennaya Komissiya po Kontrolyu za Osushchestvlenniem Inostrannykh Investitsii Odobrila Priobretenie Paketa Aktsii TMTP Niderlandskoi Kompaniei*, PortNews, Oct. 1, 2009, http://portnews.ru/news/48290\ (Russ.).

34. *Pravitel'stvennaya Komissiya po Kontolyu za Osushchestvlenniem Inostrannykh Investitsii Odobrila ryad Sdelok mezhdu Rossiiskimi i Zarubezhnymi Kompaniyami*, Finam, Oct. 1, 2009, http://www.finam.ru/analysis/newsitem4168D (Russ.).

The defendants are now accused of corporate embezzlement and money laundering on essentially the same facts as those at issue in the first criminal proceedings. The charges, spelled out in a fourteen-volume indictment, are, according to the defense and a number of commentators, quite incomprehensible. The prosecution's five-month oral presentation, consisting largely of reading out documents in their entirety into the record, has not added much clarity and has been full of comical errors.[35] It appears, however, that the managers are accused of stealing essentially all of the oil that YUKOS extracted between 1998 and 2003 (which means 350 million tons of crude oil and oil products), and then laundering the proceeds (about $30 billion). The new charges may bring up to twenty-two years of imprisonment for each defendant.[36] The defense calls the charges "large-scale falsification," and Khodorkovsky's supporters insist that the prosecution is purely political and that the process lacks any semblance of legality.

Regardless of which side is right, however, it is important to understand the potential impact of the case on Russia's legal system. The original YUKOS case, which was alleged to be politically motivated as well, produced an impact on various facets of Russian law comparable to the impact of an asteroid crashing into a planet. Most notably, the case drastically changed the landscape of Russian tax law, bringing un-codified judicial doctrines (specifically, the "bad-faith taxpayer" doctrine and its later offspring) into the forefront of legal decision-making,[37] which is extremely unusual for Russian law generally and for tax law specifically. In various YUKOS-related disputes, courts had to rule on such matters as the enforcement of domestic and foreign arbitral awards,[38] professional responsibility issues (the authorities unsuccessfully attempted to disbar a number of YUKOS's attorneys),[39] constitutional issues relating to the prolongation of the statute of limitation term in tax disputes,[40] auditors' responsibility (YUKOS's auditors, PricewaterhouseCoopers, were subject to claims under the Russian Civil Code in connection with their auditors' agreement with YUKOS).[41] YUKOS-related events gave rise to a number of European Court of Human Rights cases (most unresolved as yet) that legally

35. In one instance, the prosecution stated that a document was signed by "Victoria Road," which, as the defense pointed out, was an address.

36. *Khodorkovskogo I Lebedeva Mogut Posadit Eshcho na 22 Goda* [Khodorkovsky and Lebedev May Get 22 Years More], LENTA.RU, Jan. 15, 2008, http://lenta.ru/news/2008/01/15/more1/ (Russ.).

37. Sergey Budylin, *Dobrosovestnyy ili Nedobrosovestnyy? Konstitutsionnye Osnovy Nalogovogo Planirovaniya–Noveyshie Tendentsii* [Good Faith or Bad Faith? Constitutional Foundations of Tax Planning–Latest Tendencies], 11 ROSSIYSKAYA YUSTITTSIYA 36, 39 (2006) (Russ.).

38. RF Supreme Arbitrazh Court, Decision of 10.12.2007 N 14956/07 in case N ?40-4576/07-69-46, ?40-4581/07-69-47; RF Supreme Arbitrazh Court, Decision of 30.11.2007 N 12652/07 in case N ?67-2560/05; RF Supreme Arbitrazh Court, Decision of 06.07.2007 N 2243/07 in case N ?40-11836/06-88-35"?"; RF Supreme Arbitrazh Court Presidium, Decision of 9.06.2007 N 15954/06 in case N ?40-28164/06-60-257; RF Supreme Arbitrazh Court, Decision of 26.01.2007 N 15954/06 in case N ?40-28164/06-60-257; RF Supreme Arbitrazh Court, Decision of 18.01.2007 N 15710/06 in case N ?40-69739/05-1-362. *Under the advisement of the author, in order to properly locate the authority for some citations to Russian cases, it is necessary to diverge from the suggested Bluebook format.

39. U.S. Dept. of State, Russia: Bureau of Democracy, Human Rights, and Labor (Mar. 11, 2008), http://www.state.gov/g/drl/rls/hrrpt/2007/100581.htm.

40. RF Constitutional Court, Decision N 36-? of 18.01.2005; RF Constitutional Court, Decision of 14.07.2005 N 9-?; RF Supreme Arbitrazh Court Presidium, Decision of 04.10.2005 N 8665/04 in case N ?40-17669/04-109-241.

41. Moscow Circuit Federal Arbitrazh Court, Decision of 31.10.2008 N ??-?40/9882-08-?-?,? in case N ?40-77631/06-88-185.

form part of Russian law, as Russia has ratified the European Convention of Human Rights.[42] Although Russian law is not precedential in theory, upper-level court decisions, especially in high-profile cases, naturally teach lower courts how they should read written law, which underlines the importance of the original YUKOS case for Russian law.

The new case may have a comparable effect on the development of the law, and on perceptions regarding the rule of law in Russia more generally. With regard to both of these points, it may be helpful to explain the charges in more detail.

Under the management of Khodorkovsky and Lebedev, YUKOS was a multi-level holding structure whose head office was in Moscow. It had oil-extracting subsidiaries in various Russian regions, the most important one in Nefteyugansk. It also had shell oil-trading subsidiaries in other Russian regions, apparently selected by the level of local taxation with the idea to minimize the tax burden. In the original YUKOS case, this technique was found abusive, and the oil sales by the subsidiaries were attributed to the head office. This resulted in additional taxes charged to the head office and criminal tax evasion charges against the managers.[43]

Now, the prosecution argues that the oil sold through the trading subsidiaries was stolen by Khodorkovsky and Lebedev from YUKOS. This conclusion seems to be based on the fact that the oil was sold through shell subsidiaries rather than the head office. The payments received by the subsidiaries for the oil are interpreted as the fruit of money laundering. The defense says that those transactions were, in fact, normal economic activities carried on by the holding structure. An additional charge is that the defendants "stole" certain shares from YUKOS and laundered the proceeds. The shares were in fact sold by YUKOS subsidiaries to third parties (allegedly at too low a price). The defense contends that this too was regular economic activity.[44]

Readers are invited to review the accusations for themselves and decide to what extent they make sense.[45] If the prosecution wins the case, due to political pressure or not, the case will likely set a precedent for other cases. This means that abusive tax mitigation in Russia could effectively result not only in criminal tax evasion charges but also in corporate theft and money laundering charges. This will drastically change the understanding of what constitutes corporate theft and money laundering under Russian law.

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42. OAO NEFTYANAYA KOMPANIYA YUKOS v. Russia, Application no. 14902/04, *available at* http://www.echr.coe.int/eng; KHODORKOVSKY v. Russia, Application no. 5829/04, *available at* http://www.echr.coe.int/eng; ALEKSANYAN v. Russia, Application no. 46468/06, *available at* http://www.echr.coe.int/eng.

43. Ironically, in 2004 in the process of YUKOS bankruptcy, its main asset, Yuganskneftegaz oil-extracting company, was sold for some $10 billion to a shell company (Baykalfinansgrupp, a $300 capital company with a fictitious registered address) later acquired by state-run Rosneft. Anastasia Ivanova, *U Pokupatelya Yuganska Net Dazhe Ofisa* [Yugansk Purchaser Does Not Even Have an Office], UTRO.RU, Dec. 20, 2004, http://www.utro.ru/articles/2004/12/20/388393.shtml (Russ.). Then President Vladimir Putin explained this scheme by the need to avoid possible legal liability of Rosneft: "In this way the claims to those who later acquired the assets were practically eliminated." Interview by Spanish Media with Vladimir Putin (Feb. 7, 2006), *available at* http://eng.kremlin.ru/speeches/2006/02/07/2343_type82916_101277.shtml.

44. For some details of the parties' arguments *see* Sergey Budylin, *Khodorkovsky Trial: Who is the Crime Victim?*, 5(2) ABA SEC. OF INT'L LAW RUSS./EURASIA COMMITTEE NEWSL. 25, 28-29 (2009), *available at* http://meetings.abanet.org/webupload/commupload/IC855000/newsletterpubs/RussiaEurasiaNewsletter Spring2009%5B1%5D.pdf.

45. Obvinitel'noe zakliuchenie M.B.Khodorkovskogo I P.L.Lebedeva [Bill of Indictment of M.B Khodorkovsky and P.L.Lebedev], Feb. 14, 2009, *available at* http://khodorkovsky.ru/documents/2009/03/31/12333/ (Russ.).

The second trial of Lebedev and Khodorkovsky is being closely watched by observers interested in Rule of Law issues in Russia. When President Dmitry Medvedev, at his inauguration in May 2008, declared a war against "legal nihilism,"[46] some observers concluded that Khodorkovsky would be freed. Instead, a new trial followed. In April 2009, while the trial was already in progress, President Medvedev mentioned it in a newspaper interview. His words were befittingly neutral: he said that the result of the process should not be predictable because the court is independent.[47] Perhaps more important than what President Medvedev said, however, is that he said it to Novaya Gazeta, a mouthpiece of the liberal opposition and a consistent supporter of Khodorkovsky.

On his part, Prime Minister Vladimir Putin, answering a question on Khodorkovsky, declared, as quoted by his press secretary, that when "speaking about Khodorkovsky and other persons involved in the case[,] one should remember that they were involved in murders, and this was proved in court."[48] Neither Khodorkovsky nor Lebedev has ever been formally charged with any involvement in murder, although a YUKOS employee was indeed convicted of murder. Supporters of Khodorkovsky and YUKOS have always argued that Mr. Putin was the original source of political pressure to convict Khodorkovsky and Lebedev and to dismantle YUKOS.[49]

For the moment, the trial continues. There is no jury in the courtroom: in Russia, jury trial is available only in certain criminal cases, including murder and rape cases, but not for economic crimes. This means that the fate of Khodorkovsky and Lebedev is, at this stage at least, completely in the hands of Judge Victor Danilkin. It is hard to say to what extent Judge Danilkin is convinced by the prosecution's arguments. He invariably denies defense motions to exclude specific aspects of accusations, promising to consider defense arguments in due course. Most likely, we will not know what he is thinking until he enters a judgment. The decision will be a major event from the perspective of legal doctrine and practice in Russia, and will have significant political reverberations.

IV. INVESTMENT ARBITRATION: Renta 4 Tribunal Blazes a New Path for Asserting Jurisdiction for Claims Against Russia

Since the first known investment treaty arbitration case against the Russian Federation, decided in 1998,[50] the principal question in these disputes has concerned the scope of Russia's consent to arbitration. The issue arises from the wording of some Soviet-era Bilateral Investment Treaties (BITs) whose arbitration provisions, unlike those of later

46. *Medvedev Becomes Russian Leader*, BBC, May 7, 2008, http://news.bbc.co.uk/2/hi/europe/7386940.stm.

47. Deklaratsiya Medvedeva. God 2009 [Medvedev Declaration 2009], No. 39, NOVAYA GAZETA, Apr. 15, 2009, http://www.novayagazeta.ru/data/2009/039/01.html.

48. Konstantin Zavrazhin, *Literaturnyy Brend* [Literature Brand], No. 5013, ROS. GAZ., Oct. 8, 2009, http://www.rg.ru/2009/10/08/brend.html.

49. In his written testimony given to the European Court of Human Rights, former Prime Minister Mikhail Kasyanov states that when he asked Putin about the reasons behind the pressure on YUKOS and the arrest of Lebedev (the dialogue took place before the arrest of Khodorkovsky), Putin explained that Khodorkovsky and other YUKOS shareholders had financed electoral campaigns in defiance of Putin's instructions. *Izbiratelnaya Kampaniya YUKOS* [Electoral Campaign of Yukos], 131 KOMMERS., July 22, 2009, http://kommersant.ru/doc.aspx?DocsID=1208181 (Russ.).

50. *See* Sedelmayer v. Russian Federation, ad hoc Award (1998), *available at* http://ita.law.uvic.ca/documents/investment_sedelmayer_v_ru.pdf.

post-USSR BITs, narrowly define the limits of arbitral disputes under the BIT. These BITs limit arbitration to disputes over the "amount or mode of payment of compensation for expropriation,"[51] without mentioning the issue of whether or not an expropriation had occurred in the first place.

In the recent Award on Preliminary Objections in *Renta 4 v. Russian Federation*, an international arbitration tribunal found that these provisions did not insulate the Russian Federation from arbitration claims regarding the existence—rather than merely the quantum—of expropriation. On the other hand, the Tribunal found that a tribunal's jurisdiction to decide that question could not be based on an application of a BIT's most favored nation (MFN) clause. On both issues, the decision departed sharply from prior decisions on the subject and, some argue, relied on questionable logic. Nonetheless, the decision will undoubtedly have significant ramifications with respect to ongoing and potential claims against Russia by other investors.

A. Prior Jurisprudence

In the early case of *Sedelmayer v. Russian Federation*, the Tribunal concluded that it had jurisdiction based on the Federal Republic of Germany-USSR BIT. Sedelmayer, a German national, alleged that an expropriation by virtue of a Directive of the President of the Russian Federation[52] had forced the claimant to transfer his property to the State. The Tribunal rejected all the jurisdictional objections submitted by Russia and found that it had jurisdiction to consider the case. Although one of the eight objections asserted was that there was no expropriation at all, Russia, surprisingly, did not advance the argument that the jurisdiction of the Tribunal was limited only to disputes regarding the quantity and the technique of the compensation.[53] Thus, the Tribunal in *Sedelmayer* did not address whether the scope of investment arbitration was limited to disputes over the quantity and the technique.

The next case, *Berschader v. Russian Federation*,[54] was considered by the Stockholm Chamber of Commerce and arose under the Belgium-USSR BIT. In that case, the investor asserted that the expropriation took place after the government cancelled a construction contract and the police department forced claimant's workers to leave the site. The investor sought damages of $13.3 million for dispossession of its property. The Tribunal, in the Award on Jurisdiction of April 21, 2006, reached the conclusion that it did not have jurisdiction to arbitrate the case.

There were two major jurisdictional issues in *Berschader*. The first issue was whether the Belgium-USSR BIT gave rise to the Tribunal's jurisdiction directly. The second issue was whether Tribunal jurisdiction existed by virtue of an MFN clause, which provided that an investor was entitled to treatment no less favorable than investors of any third state.

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51. *See* Noah Rubins & Azizon Nazarov, *Investment Treaties and the Russian Federation: Baiting the Bear?*, 9 Bus. L. Int'l 103 (2008) [hereinafter Investment Treaties].

52. *See, e.g.*, Kaj Hober, Investment Arbitration in Eastern Europe 46 (2007).

53. Kaj Hober, *Investment Arbitration in Eastern Europe: Recent Cases on Expropriation*, 14 Am. Rev. Int'l. Arb. 377, 442 (2003).

54. Berschader v. Russian Federation, Arb. V 080/2004 (Stockholm Chamber of Commerce 2006), *available at* http://ita.law.uvic.ca/documents/BerschaderFinalAward.pdf [hereinafter *Berschader*].

Relying on this clause, the investor sought to import the more expansive dispute resolution provision of the Norway-Russian BIT.

The Tribunal in *Berschader* resolved both issues against the investor. First, the Tribunal concluded that, before arbitration may commence, expropriation must be found by the Russian courts. Only after an act of expropriation has been established can "the amount or mode of compensation to be paid under Article 5 of [the considered] Treaty" be adjudicated in the course of arbitration.[55] Thus, the Tribunal refused to find jurisdiction for "disputes concerning whether or not an act of expropriation actually occurred under Article 5."[56]

Second, the Tribunal analyzed the operation of the MFN clause and its extension to procedural rights, such as the right to arbitrate a particular dispute. As a starting point, the arbitrators agreed that the investor should benefit from the MFN clause—including procedural rights—as a matter of principle. As a next step, however, the Tribunal decided that, in order for the MFN clause to cover the dispute resolution provision, the text of the original BIT should clearly provide for such an operation. According to the Tribunal, "[a]n 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."[57] The Tribunal found that not to be the case. Thus, the arbitrators rejected both major jurisdictional arguments in this case.

In 2005, Russia faced another investment treaty claim, this one from Rosinvest Co. Ltd., a British company, which filed a request for arbitration before the Stockholm Chamber of Commerce based on the British-USSR BIT.[58] The claimant alleged expropriation deriving from the significant drop in value of its YUKOS shares, arguing that the Russian government undertook measures that affected the YUKOS shares on the stock market and consequently the investment of the claimant.

The UK-USSR BIT contained a dispute resolution provision virtually identical to that of the Belgium-USSR BIT. The MFN clauses were also similar. Again, as in *Berschader* case, the key issue was whether the Tribunal had jurisdiction to decide whether expropriation had occurred, rather than only the amount of compensation that would be due. As in *Berschader*, arbitrators in *Rosinvest* dealt with two main avenues to assert jurisdiction: direct application of the original BIT and the operation of the arbitration clause of a third-party BIT by virtue of the MFN clause.

In regard to the direct application of the original BIT, the *Rosinvest* Tribunal found no jurisdiction over the claims on the basis of the UK-USSR BIT. While interpreting the text of the dispute resolution provisions, the Tribunal relied on Article 31.1 of the Vienna Convention on the Law of Treaties (VCLT), which begins with "an ordinary meaning" analysis. As a starting point, the Tribunal stated that the "wording in Article 8 [the arbitration clause] presented a compromise between the UK's intention to have a wide arbi-

55. Renta 4 Tribunal, Award on Jurisdictional Objections, ¶ 22 (citing *Berschader*, *supra* note 54, ¶ 153), *available at* http://ita.law.uvic.ca/documents/Renta.pdf [hereinafter Renta 4].

56. *Id.*

57. Investment Treaties, *supra* note 51, at 109 (citing *Berschader*, *supra* note 54, ¶ 181).

58. The award on jurisdiction of April 21, 2006, in Rosinvest Co. Ltd v. Russian Federation, No. V 079/2005 (Stockholm Chamber of Commerce 2006), *available at* http://ita.law.uvic.ca/documents/RosInvestjurisdiction_decision_2007_10_001.pdf [hereinafter Rosinvest].

tration clause and the Soviet intention to have a limited one."[59] This was decisive for the Tribunal, which further stated: "[T]he Tribunal cannot see how the reference in the first jurisdictional clause expressly to the amount or payment of compensation under Articles 4 or 5 only can nevertheless be interpreted as a reference also to the earlier sections of Article 5 which deal with expropriation in general."[60]

On the question of whether it had jurisdiction by operation of the MFN clause to apply the broader dispute resolution provision of the Denmark-Russia BIT, the Tribunal first stated that the parties to arbitration agreed that the relevant article of the Denmark-Russia BIT, if applicable, would cover the claims at stake. Then the Tribunal ruled that the MFN clause allowed the British claimant to invoke the broader provision of the Denmark-Russia BIT.

The arbitrators reasoned that:

> [T]he submission to arbitration forms a highly relevant part of the corresponding protection for the investor by granting him, in case of interference with his '*use*' and '*enjoyment*,' procedural options of obvious and great significance compared to the sole option of challenging such interference before the domestic courts of the host state.[61]

Elaborating on the effect of the MFN clause, the Tribunal made a general remark that, if the MFN clause "applies to substantive protection, then it should apply even more to 'only' procedural protection."[62] Thus, the Tribunal in *Rosinvest* found jurisdiction to consider the claims on expropriation based on the MFN clause of the UK-USSR BIT, in conjunction with the dispute resolution clause of the Denmark-Russia BIT.

B. THE DECISION IN *RENTA 4 V. RUSSIAN FEDERATION*

In *Renta 4 v. Russian Federation*, claimants alleged expropriation of their assets through the takeover of the YUKOS Oil Company's assets. The Tribunal, which consisted of such prominent arbitrators as Charles N. Brower, Toby T. Landau, and Jan Paulsson, rendered an Award on Preliminary Objections on March 20, 2009. This decision came as a shockwave. Although the jurisdictional issues in *Renta 4* were essentially the same as those in *Rosinvest*, and both Tribunals ultimately found that they had jurisdiction, *Renta 4* was the mirror image of *Rosinvest*, holding that there was jurisdiction by direct application of the dispute resolution clause of the BIT, but no jurisdiction under the MFN clause.

The *Renta 4* Tribunal began with an interpretation of the dispute resolution clause in Article 10 of the Spain-Russia BIT, which referred to disputes "relating to the amount or method of payment of the compensation due under Article 6 [the expropriation clause] of this Agreement."[63] The Tribunal first rejected Russia's reliance on *Berschader*, which the arbitrators found irrelevant because it did not contain an appropriate analysis of the debated wording "concerning the amount or mode [method] of compensation."[64] For simi-

59. *Id.* ¶ 110.
60. *Id.* ¶ 112.
61. *Id.* ¶ 130.
62. *Id.* ¶ 132.
63. Bilateral Investment Treaty, Spain-Russ., Oct. 26, 1990, art. 10.
64. *Id.* (citing Spain-Russia BIT, art. 10).

lar reasons–the absence of relevant analysis–the Tribunal also declined to rely on *Sedelmayer* and *Rosinvest.*

Russia's case seemed straightforward: the claimant was seeking "to debate whether expropriation occurred"[65] while, under the dispute resolution provisions of Article 10 of the BIT, the question of whether expropriation had occurred should be determined by means other than arbitration. The Tribunal noted that an expropriation was always the predicate for any compensation. The disagreement as to "the amount . . . of . . . compensation due," therefore, might refer to not only how much but whether any compensation was due at all.[66] The Tribunal stated that "[t]he existence of the basic predicate of a remedy under Article 10 cannot be deemed outside the purview of a tribunal constituted under that very Article."[67] To hold otherwise, the Tribunal said, would "deprive the remaining text [of Article 10 of the Treaty] of its essential positive meaning."[68]

Next, the Tribunal asked whether it could interpret the scope of its own competence—in determining the amount "due"—to encompass the existence of an obligation to pay in the first place. The Tribunal pointed out that the host State's commitments should be viewed as international obligations for which the State may not act as both party and judge in measuring its own liability.[69] The Tribunal therefore concluded that the appropriate forum must be located outside the host State.

The Tribunal also heavily relied on textual analysis. It examined the text of Article 10 and found that "Article 6 defines the precondition of compensation being 'due' for the purposes of Article 10. It is an 'aspect' of Article 6 which cannot be beyond the arbitrators' reach."[70] The Tribunal concluded that it could "assess whether Russia's actions breached international law by depriving the claimants of adequate compensation for the dispossession of which they complain."[71]

The Tribunal sought to bolster its conclusion by looking at the original intent of the parties to the Treaty. The arbitrators made recourse to the negotiation history of this and similar BITs, placing particular reliance on a 1991 article published by a member of the Soviet negotiation team, Mr. R. Nagapetyants, in a Russian magazine. The article mentioned the "special practical significance" of foreign investors' ability to resort to international arbitration in cases of expropriation.[72] The arbitrators deemed it a clear statement from which it was possible to infer the Soviet Union's intention in entering into the Treaty. The Tribunal also found that BITs were concluded to attract investments and that "[i]t cannot seriously be thought that investors would be attracted by a regime that gave them access to international arbitration of the issue of the quantum of compensation but not of whether any compensation is due at all."[73]

The Tribunal was unable to ascertain Spain's intent in concluding the BIT, due to absence of credible sources, so the arbitrators referred to the Belgium-USSR BIT, whose

65. Renta 4, *supra* note 55, ¶ 29.
66. Bilateral Investment Treaty, *supra* note 63.
67. *Id.* ¶ 31.
68. Renta 4, *supra* note 55, ¶ 32.
69. *Id.* ¶ 33.
70. *Id.* ¶ 40.
71. *Id.* ¶ 45.
72. *Id.* ¶ 50.
73. *Id.* ¶ 52.

scope-of-consent clause was almost identical to that of the Spain's. The Tribunal referred to *Berschader* and concluded, based on a statement by the Belgian Minister, that "the scope of Article 10 was 'extremely broad' with respect to nationalizations and all other measures having similar effect."[74] Consequently, the Tribunal found that both parties intended for the bounds of consent to arbitration to include the question of liability for expropriation.

In exploring the second issue of whether the MFN clause provides a right to arbitration, the Tribunal first examined whether an MFN clause could be applied to jurisdictional issues at all. Russia argued in the negative, because the treatment of investments and dispute resolution are fundamentally different issues, one being substantive and the other procedural. The Tribunal, however, found "no textual basis or legal rule to say that 'treatment' does not encompass the host state's acceptance of international arbitration."[75]

The Tribunal then analyzed the exact wording of the Spain-USSR BIT. The Tribunal found that it explicitly applied the MFN promise to "fair and equitable treatment" only, unlike some other international instruments that provide for MFN application in all matters covered by the agreement. The central question, therefore, became whether "fair and equitable treatment" encompassed access to international arbitration. The arbitrators answered this question in the negative, finding that "fair and equitable treatment" related to normative standards and did not extend to "availability of international as opposed to national fora."[76]

One of the arbitrators dissented from the majority view with regard to the MFN clause. In a separate opinion, he referred to the standards of interpretation set by the VCLT, which, he wrote, justified a broader interpretation of the State's consent to arbitration. He made recourse to the Russian and Spanish versions of the BIT and concluded that the "consent to arbitrate investment treaty disputes is a form of fair and equitable treatment that a State may grant to investors."[77]

C. Conclusion

As a result of *Renta 4*, Russia can expect more claims to be brought against it under the old Soviet-era BITs, into which this decision has breathed new life. Even though the *Berschader* and *Rosinvest* decisions point in a different direction, investors may find that the case for direct application of these BITs to the merits of expropriation claims is more easily argued in light of *Renta 4*.

74. *Id.* ¶ 54.
75. *Id.* ¶ 101.
76. *Id.* ¶ 119.
77. *Id.* ¶ 23 (Charles N. Brower, separate opinion).