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PROVISIONAL APPLICATION OF THE ENERGY CHARTER AS SEEN IN THE YUKOS DISPUTE

Peter C. Laidlaw*

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INTRODUCTION

Though only a first step towards a final judgment against Russia, the 2009 Yukos Interim Awards on Jurisdiction and Admissibility were the first decisions made against the nation in an Energy Charter Treaty (ECT) arbitration.¹ Russia never formally ratified the ECT, a multilateral treaty intended to promote and protect energy-related investments

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1. Jason Waltrip, Note, *The Russian Oil and Gas Industry after Yukos: Outlook for Foreign Investment*, 17 *TRANSNAT'L L. & CONTEMP. PROBS.* 575, 581 (2008). The Yukos Arbitration, with over \$100 billion in dispute according to lawyers for the claimants, is considered the largest international arbitration case in history. See Emmanuel Gaillard et al., *Yukos Majority Shareholders Win the First Phase of their US\$100 Billion Compensation Claims against Russia*, SHEARMAN & STERLING LLP NEWS, available at <http://www.shearman.com/Yukos-Majority-Shareholders-Win-the-First-Phase-of-their-US100-Billion-Compensation-Claims-Against-Russia/> (last visited April 2, 2010).

worldwide, though it did initially sign the agreement before it floundered in the Duma, its legislature, awaiting final entry into force.² The ECT contains a controversial provision that authorizes the treaty's provisional application and enforces the substantive provisions of the treaty before its formal ratification.³ The Yukos Tribunal faced the issue of how to use the ECT's provisional application clause during a dispute raised after Russia nationalized a highly-profitable energy company owned by foreign investors, and the investors subsequently initiated an arbitration proceeding under the ECT's dispute settlement clause.⁴

The Tribunal's decision confirmed that Russia was bound by the terms of the ECT despite the absence of final ratification because Russia had the opportunity to register its lack of consent to the provisional application and never did so; and because the concept of provisional application is not fundamentally opposed by Russian national laws.⁵ This decision affected all investors who made energy-related investments in Russia prior to its formal withdrawal as a party to the ECT on Oct. 19, 2009, and these investors will be afforded the ECT's protection until Oct. 19, 2029.⁶ The Tribunal's decision fortified prior case law relating to provisional application and clearly follows customary international law as codified in the Vienna Convention on the Law of Treaties.⁷

Part I of this Comment presents the background of the Energy Charter,⁸ its provisional application,⁹ the Yukos dispute that initiated the arbitration currently pending,¹⁰ and the Tribunal's decision as it relates to provisional

2. Matthew Parish and Charles Rosenberg, *An Introduction to the Energy Charter Treaty*, 20 AM. REV. INT'L ARB. 191, 191 (2009).

3. *See id.* at 198 n.37.

4. Alex M. Niebruegge, *Provisional Application of the Energy Charter Treaty: The Yukos Arbitration and the Future Place of Provisional Application in International Law*, 8 CHI. J. INT'L L. 355, 357 (2007).

5. Elliot Glusker, *Arbitration Hurdles Facing Foreign Investors in Russia: Analysis of Present Issues and Implications*, 10 PEPP. DISP. RESOL. L.J. 595, 615 (2010).

6. *Id.*

7. *Id.*

8. *See infra* Part I.A.

9. *See infra* Part I.B.

10. *See infra* Part I.C.

application.¹¹ Part II identifies the problems of provisional application of the Energy Charter Treaty either in part or in whole.¹² Part III analyzes the Tribunal's decision,¹³ and Part IV proposes a solution to the problem of provisional application: that treaty drafters include much more specific delineations of pre-entry into force obligations for signatory countries.¹⁴

I. BACKGROUND

A. *A Summary of the Energy Charter Treaty (ECT)*

The Energy Charter Treaty (ECT) is a "multilateral treaty that provides a multilateral framework for energy cooperation ensuring the liberalization of the energy market including western and eastern, formerly communist [s]tates."¹⁵ By establishing a legal framework that promotes long-term cooperation in the energy sector in accordance with the objectives and principles of the European Energy Charter,¹⁶ it promotes foreign direct investment in the energy market by affording to investors and investments the protections of international law.¹⁷

The ECT promotes five primary objectives: (1) protection and encouragement of foreign energy investments based on the extension of national treatment of most-favored nation provisions, (2) free trade in energy-related goods based on World Trade Organization guidelines, (3) freedom of energy transmission, (4) energy efficiency and heightened environmental protection, and (5) a mechanism for the resolution of investment disputes.¹⁸ Despite its range of

11. See *infra* Part I.D.

12. See *infra* Part II.

13. See *infra* Part III.

14. See *infra* Part IV.

15. Gerhard Hafner, *The Energy Charter Treaty*, in INTERNATIONAL INVESTMENT LAW FOR THE 21ST CENTURY 593, 599 (2009).

16. Energy Charter Treaty art. 2, Dec. 17, 1991, 2080 U.N.T.S. 100, 34 I.L.M. 360 [hereinafter ECT]. The European Energy Charter is a non-binding declaration by over fifty European states to promote energy sector cooperation after the fall of the USSR. See also Energy Charter Secretariat, *The Energy Charter Treaty: A Reader's Guide* (2002), available at http://www.encharter.org/fileadmin/user_upload/Publications/ECT_Guide_ENG.pdf (last visited Oct. 17, 2011).

17. Parish and Rosenberg, *supra* note 2, at 191.

18. Hafner, *supra* note 15, at 599.

goals, experts consider the ECT's provisions protecting foreign investment to be the cornerstone of the treaty.¹⁹ These provisions divide investment protection into two categories: pre-investment, where investments are afforded a "soft" regime of 'best endeavor obligations,' and post-investment, where there is a "hard" regime . . . with binding obligations for the contracting states similar to the investment protection provisions of the North American Free Trade Agreement"²⁰

Parties seeking cooperation on energy between Eastern and Western Europe produced the ECT in order to reconcile two inconvenient realities: Eastern Europe was energy-rich but cash poor and therefore in need of foreign investment to extract, market, and transport its products, while Western Europe needed to diversify its energy sources and possessed the capital to do so.²¹ But because Eastern Europe was still restructuring its economies after the fall of the Soviet Union, backers of the ECT considered "quick economic integration of energy markets in the former East and West . . . vital to the restructuring and reform of the former communist economies"²² Therefore, the ECT contains a clause authorizing its "provisional application."²³ Provisional application of a treaty occurs when its obligations are imposed on a signatory state prior to full ratification by the state government.²⁴

B. Provisional Application and the ECT

Conclusion of a treaty has three parts: signature, ratification, and entry into force.²⁵ The act of signing a treaty does not create a legal duty on the signatory to ratify the treaty, nor does it—without something more—create a duty to abide by the provisions of the treaty.²⁶ As a general

19. Kaj Hober, *Investment Arbitration and the Energy Charter Treaty*, 1 J. INT'L DISPUTE SETTLEMENT 153, 155 (2010).

20. *Id.*

21. *Id.* at 154.

22. Ulrich Klaus, *The Gate to Arbitration – The Yukos Case the Provisional Application of the Energy Charter Treaty in the Russian Federation*, 2 TRANSNATIONAL DISPUTE MANAGEMENT (2005), available at <http://www.transnational-dispute-management.com/article.asp?key=498> (last visited Nov. 18, 2010).

23. See ECT, *supra* note 16, art. 45.

24. Hafner, *supra* note 15, at 594.

25. Niebruegge, *supra* note 4, at 357.

26. *Id.*

principle of international law, treaties also do not have legal effect before their entry into force.²⁷ Provisional application is meant to resolve the difficulties that arise as a result of what is oftentimes a significant delay between when a treaty is signed and when it is ratified by member nations and entered into force.²⁸ Though failure to ratify a treaty would normally preclude even the discussion of whether a state was bound by the obligations of the treaty, the theory of provisional application is a work-around solution that mandates compliance with treaty terms pre-ratification.²⁹

Provisional application is a relatively common practice for treaties demanding immediate enforcement, such as those to provide disaster relief or war support, though it has only recently seen use in investment treaties.³⁰ The Vienna Convention of 1969 on the Law of Treaties (VCLT) first explicitly addressed the idea of provisional application.³¹ In Article 25 (Provisional Application), the VCLT provided a broad background for provisional application, affording treaty parties much discretion in its use:

1. A treaty or a part of a treaty is applied provisionally pending its entry into force if:
 - (a) the treaty itself so provides; or
 - (b) the negotiating States have in some other manner so agreed.
2. Unless the treaty otherwise provides or the negotiating States have otherwise agreed, the provisional application of a treaty or a part of a treaty with respect to a State shall be terminated if that State notifies the other States between which the treaty is being applied provisionally of its intention

27. *Id.*

28. Matthew Belz, *Provisional Application of the Energy Charter Treaty: Kardassopoulos v. Georgia and Improving Provisional Application in Multilateral Treaties*, 22 EMORY INT'L. L. REV. 727, 728–29 (2008).

29. William Spiegelberger, *The Enforcement of Foreign Arbitral Awards in Russia: An Analysis of the Relevant Treaties, Laws, and Cases*, 16 AM. REV. INT'L ARB. 261, 271 n.48 (2005).

30. Belz, *supra* note 28, at 728. The author notes that “[n]egotiating states typically provide for such application when matters must be urgently dealt with or the parties are faced with or act in anticipation of an international crisis and need to bypass the time-consuming practice of concluding treaties.” *Id.* at 728 n.7.

31. Niebruegge, *supra* note 4, at 355 n.3

not to become a party to the treaty.³²

The VCLT refers only to the methods for making the treaty applicable and for terminating this application rather than delineating the scope of provisional application; “it neither implies any restriction of the scope of the treaty nor does it define the method through which the provisional application is launched except that it differs from that required for the entry into force.”³³

Controversially, provisional application of a treaty creates a dilemma where treaty obligations are given effect prior to a country’s formal ratification or accession to the treaty.³⁴ Provisional application of a treaty is generally utilized in one of two situations.³⁵ The first scenario involves a treaty created in response to some form of international crisis, where “immediate and decisive action may be necessary to avert catastrophe.” In this case, ratification delays are not acceptable and provisional application works as a way around the delay.³⁶

The second scenario involves a treaty where quick, broad participation and enforcement is necessary in order for it to be effective.³⁷ In this case, pre-ratification application is justified by the fact that some states may want to undertake their responsibilities immediately, that those participating in the negotiations are certain the treaty will eventually be ratified, or that the negotiators are attempting to work around other political hurdles.³⁸

Despite the specifications in the VCLT, provisional application remains an amorphous and vague doctrine often characterized by ambiguity.³⁹ This ambiguity arises from the key consideration of whether provisional application applies to the treaty as a whole or is limited to certain provisions in a more piece-meal approach.⁴⁰ Though relatively undefined, provisional application “can be best understood as an attempt

32. Vienna Convention on the Law of Treaties [hereinafter VCLT]. art. 25, 1155 U.N.T.S. 331, 339 (1969).

33. Hafner, *supra* note 15, at 594.

34. Hober, *supra* note 19, at 164.

35. Niebruegge, *supra* note 4, at 358.

36. *Id.*

37. *Id.*

38. Hober, *supra* note 19, at 164.

39. Hafner, *supra* note 15, at 594.

40. *Id.* at 595.

to solve the collective action problem created by the gap between signature and entry into force of an international treaty.”⁴¹ Provisional application solves the problem of a country capturing treaty benefits at the time of signing without incurring the obligations that accompany ratification.⁴² By forcing signatory parties to face the costs and ramifications of treaty obligations immediately upon signature, provisional application is an incentive for a country to ratify the treaty in full without delay.⁴³

As in most treaties that utilize provisional application, the ECT expands on the language of the VCLT with an entire article discussing the scope of its provisional application.⁴⁴ However, the ECT still does not address the scope of the provisional application, beyond allowing states an opt-out clause if the treaty is in conflict with national law.⁴⁵ Article 45 of the ECT, the section containing the guidelines for provisional application, begins by providing that:

(1) Each signatory agrees to apply this Treaty provisionally pending its entry into force for such signatory in accordance with Article 44, to the extent that such provisional application is not inconsistent with its constitution, laws or regulations.⁴⁶

In brief, Article 45(1) applies the treaty provisionally so long as application is not inconsistent with the laws, constitution, or regulations of the country; however, much uncertainty lies within this section of the ECT.⁴⁷ Pursuant to Article 31 of the Vienna Convention of 1969 on the Law of Treaties,⁴⁸ the first step in determining the meaning of an article is to look at its ordinary meaning. Under this method, the language “to the extent” operates *ipso jure*.⁴⁹

[Plain meaning] can result in a partial provisional application of the ECT, namely to the extent the provisions of the ECT are not inconsistent with the signatory’s constitution, laws, or regulations. This *ipso*

41. Niebruegge, *supra* note 4, at 355.

42. *Id.* at 359.

43. *Id.*

44. Hafner, *supra* note 15, at 597.

45. *Id.*

46. ECT, *supra* note 16, art. 45(1).

47. Niebruegge, *supra* note 4, at 360.

48. VCLT, *supra* note 32, art. 31.

49. Hafner, *supra* note 15, at 601.

jure effect is also confirmed by practice: the United Kingdom recognized that, due to the ‘to the extent clause’ of Article 45(1) ECT, the Russian Federation was obliged to apply the ECT provisionally only to the extent that such provisional application was not inconsistent with its constitution, laws, or regulations.⁵⁰

Two interpretations of the language of 45(1) have evolved.⁵¹ One approach applies the ECT provisionally only if the national laws of the signatory state allow provisional application of international treaties and these national laws have been followed.⁵² In this case, only the legal concept of provisional application must be compatible with national law, rather than every term of the ECT.⁵³ So long as national laws are compatible with provisional application of the terms of the treaty, no further inquiry is necessary to determine whether the treaty’s other articles are in agreement with national laws.⁵⁴

That is not the case with the second approach to the interpretation of Article 45(1), which requires not only that national laws of the signatory state allow the provisional application of the treaty, but that the treaty’s *terms* comport with national laws before the treaty can be provisionally applied.⁵⁵ According to one scholar, this second approach seems more likely correct because the purpose “of a limitation in provisional application, as in Article 45(1) of the ECT, is to avoid possible internal conflicts between the treaty’s provisions and national regulations during a transitional period.”⁵⁶

The controversy stemming from Article 45(1)’s provisional application of treaty terms is whether it deems parliamentary ratification useless; if a signatory state must comply with a treaty’s terms after signing, why go through the lengthy and formal process of ratification?⁵⁷ The tribunal

50. *Id.*

51. Klaus, *supra* note 22.

52. *Id.*

53. *Id.*

54. See Hafner, *supra* note 15, at 601.

55. Klaus, *supra* note 22.

56. *Id.*

57. See Noah Rubins and Azizjon Nazarov, *Investment Treaties and the Russian Federation: Baiting the Bear?*, 9 BUS. L. INT’L 100, 111 (2008).

in *Petrobart v. Kyrgyzstan*⁵⁸ gave minor consideration to this issue,⁵⁹ holding that “Article 45(1) of the ECT meant that the signature document . . . was already sufficient for the treaty to enter into effect . . . and that this accession remained in force indefinitely.”⁶⁰

Article 45(2) allows a signatory to opt out of provisional application by notifying other signatory countries.⁶¹ By exercising this right, a country and its investors may not claim the benefits of provisional application:⁶²

2(a) Notwithstanding paragraph (1) any signatory may, when signing, deliver to the Depositary a declaration that it is not able to accept provisional application. The obligation contained in paragraph (1) shall not apply to a signatory making such a declaration. Any such signatory may at any time withdraw that declaration by written notification to the Depositary.

(b) Neither a signatory which makes a declaration in accordance with subparagraph (a) nor Investors of that signatory may claim the benefits of provisional application under paragraph (1).

(c) Notwithstanding subparagraph (a), any signatory making a declaration referred to in subparagraph (a) shall apply Part VII provisionally pending the entry into force of the Treaty for such signatory in accordance with Article 44, to the extent that such provisional application is not inconsistent with its laws or regulations.⁶³

This approach differs strongly from that of 45(1) because “[p]ursuant to this provision, any signatory State may declare that it does not accept the provisional application of the ECT.

58. *Petrobart Ltd. v. The Kyrgyz Republic*, Arbitral Award of the Arbitration Institute of the Stockholm Chamber of Commerce, SCC Case No. 126/2003 (March 29, 2005) [hereinafter *Petrobart Award*]. A tribunal is a court with special jurisdiction generally based on multilateral agreements and with the purpose of hearing claims often relating to international issues. See, e.g., Benedict Kingsbury, *Foreword: Is the Proliferation of International Courts and Tribunals a Systemic Problem?*, 31 N.Y.U J. INT'L L. & POL. 679 (1999).

59. Rubins and Nazarov, *supra* note 57, at 111 (“The claimant in the case was a company created under the laws of Gibraltar, which initiated . . . arbitration against Kyrgyzstan under the ECT in relation to gas supplies in Central Asia.”).

60. *Id.*; see also *Petrobart Award*, *supra* note 58.

61. ECT, *supra* note 16, art. 45(2).

62. Niebruegge, *supra* note 4, at 360.

63. ECT, *supra* note 16, art. 45(2).

The expression ‘may’ expresses a right or option that can be exercised, but does not impose any obligation on the State.”⁶⁴

Whereas Article 45(1) passively obliges the nation upon signing, without necessitating further action, a nation must actively exercise Article 45(2) before it takes effect.⁶⁵ Article 45(2) was designed specifically to allow a signatory nation explicitly to reject provisional application and thereby excuse itself from the obligation incurred in Article 45(1).⁶⁶ Though several signatory states utilized this opt-out provision, the Russian Federation was not one of them.⁶⁷ By July 2006, only five countries—Australia, Belarus, Iceland, Norway, and the Russian Federation—had yet to ratify the ECT, and of those five, Australia, Iceland, and Norway all exercised the opt-out provision in Article 45(2).⁶⁸ Clearly, Articles 45(1) and 45(2) represent two different approaches to provisional application.⁶⁹

Even if a nation accepts provisional application of the treaty, Article 45(3) gives that signatory the right to terminate provisional application at any time. However, despite terminating application of the treaty, the signatory must continue to abide by the provisions of the ECT relating to investment promotion and protection and dispute settlement for the twenty years following termination.⁷⁰ The text of 45(3) reads:

(3)(a) Any signatory may terminate its provisional application of this Treaty by written notification to the Depositary of its intention not to become a Contracting Party to the Treaty. Termination of provisional application for any signatory shall take effect upon the expiration of 60 days from the date on which such signatory’s written notification is received by the Depositary.

(b) In the event that a signatory terminates provisional application under subparagraph (a), the obligation of the

64. Hafner, *supra* note 15, at 601.

65. ECT, *supra* note 16, arts. 45(1), 45(2).

66. Hafner, *supra* note 15, at 602.

67. Frederik Erixon, *European Center for International Political Economy Policy Brief 7* 1, 10 (2008), available at <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.172.1403&rep=rep1&type=pdf>.

68. Niebruegge, *supra* note 4, at 360.

69. *Id.*

70. *Id.*; see also ECT, *supra* note 16, art. 45(3).

signatory under paragraph (1) to apply Parts III and V with respect to any Investments made in its Area during such provisional application by Investors of other signatories shall nevertheless remain in effect with respect to those Investments for twenty years following the effective date of termination, except as otherwise provided in subparagraph (c).⁷¹

Provisional application ends under Article 45(3)(a) when the signatory state submits written notification of its desire not to become a party to the treaty.⁷² Until then, Article 45(3)(b) bestows a range of benefits to investors and investments.⁷³ Despite a signatory's notification that it intends to terminate its application of the ECT, the terminating signatory must still apply Part III (Promotion and Protection of Investment) and Part V (Dispute Settlement) of the ECT to investments made prior to termination for twenty years following the date of termination.⁷⁴ This provision implies that the treaty as a whole applies provisionally for an indefinite period of time unless terminated by the signatory, in which case certain provisions relating to protection of prior investments remain in effect for twenty years.⁷⁵

The inclusion of Article 45 in the ECT triggered provisional application of its rules by all signatory parties in December 1994 until the ECT's entry into force in April 1998, unless a signatory state explicitly rejected provisional application.⁷⁶ After the treaty's entry into force in April 1998, it still required provisional application to signatory states that had not yet ratified it.⁷⁷ Russia was one of these states. Having initiated the ratification process in 1996 with the ECT's introduction to the State Duma and Parliamentary hearings in 1998, the Duma continually postponed ratification due to concerns about certain provisions of the treaty.⁷⁸

Because it initially signed the ECT, "Russia and the other signatories . . . agreed to apply [the ECT] provisionally

71. ECT, *supra* note 16, art. 45(3).

72. Erixon, *supra* note 67, at 12.

73. ECT, *supra* note 16, art. 45(3)(b).

74. Erixon, *supra* note 67, at 12.

75. *Id.* This is the main focus of the Yukos Tribunal. See *infra* Part III.

76. Hober, *supra* note 19, at 166.

77. *Id.*

78. *Id.*

pending its entry into force . . . to the extent that such provisional application [was] not inconsistent with its constitution, laws or regulations.”⁷⁹ Russia did not enter a declaration of non-application under ECT Article 45(2), therefore the treaty required Russia to accept its application on a provisional basis.⁸⁰

C. *The Yukos Dispute*

The Yukos Arbitration, the largest arbitration in history based on amount of money in controversy and a case at least initially centering on the issue of provisional application of the ECT,⁸¹ has its roots in the organization of the Yukos Oil Company in 1993 under the laws of the Russian Federation.⁸² Yukos was a joint stock corporation that had been publicly-traded since the privatization of state-owned energy companies after the fall of the USSR.⁸³ The Russian Federation, initially the sole shareholder in Yukos, sold its holdings in 1995 and 1996 to stave off a debt crisis.⁸⁴ A group of investors headed by Mikhail Khodorkovsky and Platon Lebedev, Russian citizens, purchased approximately fifty-one percent of the stock through a Gibraltar-based holding company called Menatep.⁸⁵ The privatization of Yukos was just one part of a massive effort towards de-nationalization led by Boris Yeltsin in the hope of creating a more Western-style, free-market economy.⁸⁶ Privatization resulted in the rise of oligarchs like Khodorkovsky, who led Yukos to the position of top oil producer in Russia.⁸⁷ For ten years, leaders of the highly-profitable Yukos wielded significant economic and political power⁸⁸ due to Yukos’ quick growth into

79. Spiegelberger, *supra* note 29, at 271 n.48 (internal citations omitted).

80. *Id.*

81. *See, e.g.*, Belz, *supra* note 28, at 727.

82. *Id.*

83. Niebruegge, *supra* note 4, at 362.

84. *Id.* at 363. *See also* Waltrip, *supra* note 1, at 581 (noting that Khodorkovsky initially loaned the Russian government over \$300 million and then acquired control when the Russian government defaulted on the loan).

85. Niebruegge, *supra* note 4, at 363.

86. Brenden Marino Carbonell, Comment, *Cornering the Kremlin: Defending Yukos and TNK-BP from Strategic Expropriation by the Russian State*, 12 U. PA. J. BUS. L. 257, 261 (2009).

87. *Id.*

88. Niebruegge, *supra* note 4, at 363.

a multinational corporation.⁸⁹ Yukos' highest levels of production made it one of the world's largest private oil companies in terms of reserves and market capitalization.⁹⁰ In 2003, it boasted over 600 subsidiaries, an average daily output of more than 1.6 million barrels of oil, \$2 billion in distributed dividends, and \$18 billion in assets.⁹¹ Mikhail Khodorkovsky, Yukos' chairman, was considered Russia's richest man.⁹²

After Vladimir Putin became president of Russia in 1999, he made his feelings toward the private powerful energy companies clear; these feelings were expressed by his deputy head of the Presidential Administration, Vladislav Surkov, who commented that "[the new administration] will not allow a small group of companies to be the power in the country where they permeate the state apparatus."⁹³ President Putin viewed energy resources as "an opportunity for Russia to recover economically and re-emerge on the geopolitical stage as a superpower. The oil and natural gas should further the revitalization of the entire country."⁹⁴

The Putin administration exerted great control over Russia's energy sector, enforcing a stiff period of regulation that marked a "stark contrast to the free-wheeling laissez-faire attitude characteristic of the Yeltsin years."⁹⁵ Beginning in 2003, Putin's administration sought to achieve this goal of returning major energy sector companies to state control by harassing those involved with Yukos.⁹⁶ In July, the government arrested Lebedev, the president of Menatep, on charges of illegally acquiring an investment in a state-owned fertilizer company. "Over the next month, Russian

89. Matteo Winkler, *Arbitration Without Privity and Russian Oil: The Yukos Case Before the Houston Court*, 27 U. PA. J. INT'L ECON. L. 115, 115 (2006).

90. Waltrip, *supra* note 1, at 582.

91. Winkler, *supra* note 89, at 116.

92. Elliot Glusker, *Arbitration Hurdles Facing Foreign Investors in Russia: Analysis of Present Issues and Implications*, 10 PEPP. DISP. RESOL. L.J. 595, 611 (2010).

93. Phillip Hanson, *Observations on the Costs of the Yukos Affair to Russia*, 46 EURASIAN GEOG. & ECON. 481, 483 (2005) (cited in Carbonell, *supra* note 86, at 259).

94. Carbonell, *supra* note 86, at 263.

95. *Id.* at 280.

96. Catherine Belton, *The Arrest that Proved a Turning Point*, *Moscow Times* 1 (Oct. 25, 2006) (cited in Niebruegge, *supra* note 4, at 363).

authorities continued to arrest a number of former and current employees of Menatep, Yukos, and subsidiaries.⁹⁷ In October, authorities arrested Khodorkovsky for fraud and tax evasion, charges that were widely believed to stem from Khodorkovsky's support of Putin's political rivals, and from the possibility that Exxon Mobil had interest in buying a holding in Yukos from Menatep.⁹⁸

The Russian government also confronted Yukos about tax deficiencies⁹⁹ that were seen as largely politically motivated.¹⁰⁰ The Russian Ministry of Finance in December 2003 made a series of tax assessments that would eventually total \$27.5 billion, based on purportedly deficient tax payments from 2000 to 2004.¹⁰¹ Authorities froze over five billion dollars of assets held by several principal Yukos investors,¹⁰² and in November 2004, the bailiffs of the Ministry of Justice announced an auction of Yukos' primary production arm, Yuganskneftegaz (YNG), responsible for over sixty percent of Yukos' oil production.¹⁰³ The Ministry of Justice announced that it was only seeking half of the actual market price for YNG.¹⁰⁴

In order to halt the YNG auction, the managers of Yukos filed a bankruptcy action in Houston, Texas.¹⁰⁵ United States bankruptcy laws, among the most debtor-favorable in the world, gave jurisdiction to companies with worldwide assets and could prevent creditors from appropriating those assets.¹⁰⁶ Though the judge initially granted an injunction forbidding various corporate entities and "those persons in active concert or participation with them"¹⁰⁷ from

97. *Id.*

98. *Id.*

99. *Id.*

100. Glusker, *supra* note 92, at 611.

101. Niebruegge, *supra* note 4, at 363.

102. Waltrip, *supra* note 1, at 582–83.

103. Winkler, *supra* note 89, at 117.

104. *Id.*

105. Carbonell, *supra* note 86, at 267.

106. Dmitry Golobolov and Joseph Tanega, *Yukos Risk, the Double-Edged Sword: A Case Note on International Bankruptcy Litigation and the Transnational Limits of Corporate Governance*, 3 N.Y.U. J. L. & BUS. 557, 582 (2006).

107. *Yukos Oil Co. v. Russian Federation (In re Yukos Oil Co.)*, 320 B.R. 130, 138 (Bankr. S.D. Tex. 2004); *see also* Golobolov and Tanega, *supra* note 106, at 596 ("Judge Clark entered a TRO enjoining certain entities from taking any actions with respect to YNG stock, including participating in the auction.").

participating in the sale, the auction nevertheless continued as planned, with a previously unknown company called Baikalfinansgroup winning the auction and subsequently merging with Rosneft, the Russian state-owned energy company.¹⁰⁸ Baikalfinansgroup, thought to be a front company and only recently registered in a grocery shop in a small Russian town, paid \$9.4 billion for an asset that was valued at \$60 billion by the London Stock Exchange,¹⁰⁹ and between \$14.7 billion and \$21.1 billion by private financiers.¹¹⁰

Because it appeared that the entire auction was a blatant attempt by the Russian government to regain control over Yukos, there was much international criticism of the sale.¹¹¹ Fueling this criticism is the fact that after acquisition by Rosneft, the tax claims against YNG were reduced by nearly \$4 billion;¹¹² “these events strengthen the perception that the actions against Yukos were not an issue of legitimate tax liability, but rather part of a plan by the Russian government to consolidate control over the energy sector.”¹¹³

Yukos continued to seek protection under the bankruptcy laws of the United States,¹¹⁴ but the court in Texas eventually granted Russia’s motion to dismiss the case based on the totality of the circumstances, including Yukos’ inability to reorganize without the cooperation of the Russian government; the fact that it had only recently begun to hold

Those entities included the three Russian companies registered to bid at the auction and the six banks that had announced interest in funding a purchaser’s bid. *Id.*

108. Carbonell, *supra* note 86, at 267; see also Erin E. Arvedlund and Steven Lee Meyers, *An All-but-Unknown Company Wins a Rich Russian Oil Stake*, NY TIMES A1 (Dec. 20, 2004) (“The mystery surrounding the winner -- a company called the Baikal Finans Group that is registered in Tver, a medium-size city 170 miles northwest of Moscow -- immediately raised suspicion among industry analysts” and an analyst commented after the auction ended that “the surprise winning bidder, Baikal Finans Group, is either a front for Gazprom or a state-friendly company . . . [or] a combination of state and state-friendly interests.”).

109. The Economist, “After Yukos: The Far-Reaching Legacy of the Yukos Affair,” May 10, 2007, available at <http://www.economist.com/node/9167397>.

110. Niebruegge, *supra* note 4, at 365.

111. Golobolov and Tanega, *supra* note 106, at 603–04 (noting that the sale was “mysterious” and undermined confidence in investing in Russia).

112. Niebruegge, *supra* note 4, at 365.

113. *Id.*

114. Carbonell, *supra* note 86, at 267. See also Winkler, *supra* note 89, at 119–21.

assets in the United States and initiated proceedings in multiple fora; the complexity of applying numerous foreign statutes involved in such a complex situation; lack of personal jurisdiction over most foreign officials involved; and the necessity of cooperation by the Russian government to successfully adjudicate the matter, which did not seem forthcoming.¹¹⁵

Seeking to find remuneration for an asset assertedly expropriated by the Russian government, Menatep's major subsidiaries sent notice to Russia on November 2, 2004 that triggered the ECT's mandatory three-month conciliation period.¹¹⁶ Once the conciliation period ended, the subsidiaries filed a notice of arbitration with Russia, filing a \$28.3 billion claim for compensation due as a consequence for the actions taken by the Russian government.¹¹⁷ The arbitration proceeded under the UNCITRAL Arbitration Rules and was supervised by the Permanent Court of Arbitration in The Hague.¹¹⁸ Menatep's primary claim was that Russia's actions against Yukos, especially the forced sale of YNG, were tantamount to expropriation.¹¹⁹ The threshold issue for the panel of arbitrators to decide was whether Russia was required to abide by the provisions of the ECT as a whole.¹²⁰ The issue was the subject of two rounds of written pleadings and a hearing in The Hague in 2008, and the tribunal came to a decision near the end of 2009.¹²¹ Because only a brief summary of the decision was initially released, there was much speculation about the substance of the award, the first ECT award against Russia.¹²²

115. Carbonell, *supra* note 86, at 267. See also Winkler, *supra* note 89, at 119–21.

116. Niebruegge, *supra* note 4, at 365; see also ECT, *supra* note 16, art. 26(3).

117. Niebruegge, *supra* note 4, at 365–66.

118. *Id.* at 366; see also International Institute for Sustainable Development, *Investment Treaty News* 4 (Feb. 22, 2005) available at http://www.iisd.org/pdf/2005/investment_investsd_feb22_2005.pdf.

119. Niebruegge, *supra* note 4, at 366.

120. *Id.*

121. Alison Ross, *Lawyers React to Yukos Awards*, 5 GLOBAL ARBITRATION REV. 11, 11 (2010).

122. *Id.*

D. *The Tribunal's Decision on Provisional Application*

On February 1, 2010, counsel for claimant Menatep unilaterally published the entire arbitral decision despite Russia's reluctance toward making the award public.¹²³ Though the tribunal addressed multiple preliminary issues in the arbitration,¹²⁴ only its decision regarding provisional application of the ECT will be addressed in this Comment.

With regard to whether Article 45 of the ECT required that Russia provisionally apply the terms of the treaty to the claimants' investments, the Tribunal used a three-step analysis to hold that Russia must protect the investments as it would have under the ECT.¹²⁵ As a preliminary matter, the Tribunal noted that the parties agreed to certain facts: first, that Russia signed the ECT on December 17, 1994 and that it was discussed in parliament but never ratified; second, that Russia notified the ECT countries of its intention not to become a party on August 20, 2009, effectively terminating its provisional application on October 18, 2009; and third, that Russia was still bound by ECT 45(3)(b) to give provisional application of Parts III and V—the sections relating to protection of previous investments—until October 18, 2029 of the ECT to any investments made in Russia before the date of termination of provisional application.¹²⁶

The Tribunal began its analysis by considering whether Russia was obligated to prepare a declaration under Article 45(2) of the ECT in order to make use of Article 45(1), the clause of the ECT that proscribes provisional application

123. *Id.*

124. *See, e.g., id.*

125. Dr. Chiara Giorgetti, *The Yukos Interim Awards on Jurisdiction and Admissibility Confirms Provisional Application of the Energy Charter Treaty*, 14 AMERICAN SOCIETY OF INTERNATIONAL LAW INSIGHT ISSUE 23 (Aug. 3, 2010).

126. *Yukos Universal Ltd. v. Russian Federation*, Interim Award on Jurisdiction and Admissibility, PCA Case No. AA 227 (Nov. 30, 2009), available at <http://ita.law.uvic.ca/documents/YULvRussianFederation-InterimAward-30Nov2009.pdf>; *Hulley Enterprises Ltd. v. Russian Federation*, Interim Award on Jurisdiction and Admissibility, PCA Case No. AA 226 (Nov. 30, 2009), available at <http://ita.law.uvic.ca/documents/HELvRussianFederation-InterimAward-30Nov2009.pdf>; *Veteran Petroleum Trust v. Russian Federation*, Interim Award on Jurisdiction and Admissibility, PCA Case No. AA 228 (Nov. 30, 2009), available at <http://ita.law.uvic.ca/documents/VPLvRussianFederation-InterimAward-30Nov2009.pdf> [hereinafter *VPT Award*]. The Tribunal is hearing these three cases together and issued an identical decision for each case. *Id.*; see also Giorgetti, *supra* note 125.

when it is inconsistent with the constitution, laws, or regulations of the signatory state (known as the Limitation Clause).¹²⁷ Article 45(2) states that a signatory may, at the time of signing, notify other signatory parties that it is not able to accept provisional application.¹²⁸ The Tribunal agreed with Russia that this language did not preclude a state from arguing that its laws were against provisional application when the state had not submitted a declaration under 45(2).¹²⁹

The Claimants argued that, pursuant to the plain meaning of the ECT, Article 45(1) established the principle of provisional application and 45(2) established the “procedure according to which a signatory State may opt out of the concept of provisional application.”¹³⁰ The Tribunal, however, declined to follow this suggestion and instead found that Articles 45(1) and 45(2) presented two separate regimes of provisional application.¹³¹ Article 45(1) applied “only in case of inconsistency between the treaty provisions and a signatory’s constitution, laws, or regulations,” and did not require a declaration. Section 45(2), on the other hand, applied when a state wanted to prevent provisional application for political or other reasons, and did require an express declaration.¹³²

The Tribunal made this determination first by using Article 31 of the VCLT¹³³ to examine the plain meaning of Article 45.¹³⁴ Though both the Claimant and Respondent made arguments based on the plain meaning of the law, the Tribunal found that respondent Russia’s approach was more faithful to the object and purpose of the ECT.¹³⁵ In addition, six signatory states had already relied on the Limitation Clause in Article 45(1) without delivering a formal notice to

127. VPT Award, *supra* note 126, para. 244; *see also* Giorgetti, *supra* note 125.

128. ECT, *supra* note 16, art. 45(2).

129. VPT Award, *supra* note 126, para. 264.

130. *Id.* at para. 251.

131. *Id.* at para. 250.

132. *Id.*

133. Vienna Convention on the Law of Treaties art. 31, 1155 U.N.T.S. 331, 8 I.L.M. 679 (1969) (“A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.”).

134. VPT Award, *supra* note 126, para. 262.

135. *Id.* at para. 263.

the ECT governing body as required by Article 45(2).¹³⁶ Beyond this evidence of state practice, the Tribunal also found support in the recent ICSID arbitration decision in the *Kardassopoulos* case.¹³⁷ There, the Tribunal noted:

There is no necessary link between paragraphs (1) and (2) of Article 45. A declaration made under paragraph (2) may be, but does not have to be, motivated by an inconsistency between provisional application and something in the State's domestic law; there may be other reasons which prompt a State to make such a declaration. Equally, a State whose situation is characterized by such inconsistency is entitled to rely on the proviso to paragraph (1) without the need to make, in addition, declaration under paragraph (2). The Tribunal is therefore unable to read into the failure of either State to make a declaration of the kind referred to in Article 45(2) any implication that it therefore acknowledges that there is no inconsistency between provisional application and its domestic law.¹³⁸

Once it had determined that the approaches dictated by Articles 45(1) and 45(2) were independent of one another,¹³⁹ the Tribunal addressed its next issue regarding provisional application: whether Article 45(1), the Limitation Clause, required states to inform the other signatories that it could not apply the ECT provisionally.¹⁴⁰ Both Claimant and Respondent agreed that Respondent Russia had not made such a declaration or given prior notice, so "an affirmative answer to this question would dispose of the Article 45 issue in favor of Claimant."¹⁴¹

To support its case, Russia pointed to other countries that previously relied on the Limitation Clause of Article 45(1) due to a disagreement between national laws and the obligations of provisional application without making a formal declaration.¹⁴² In response, Claimant argued that

136. *Id.* at para. 265. The six countries were Austria, Luxembourg, Italy, Romania, Portugal, and Turkey. *Id.*

137. *Kardassopoulos v. Georgia*, ICSID Case No. ARB/05/18, Decision on Jurisdiction, ¶ 228 (July 6, 2007) (quoted in *VPT Award*, *supra* note 126, para 269.).

138. *Id.*

139. *VPT Award*, *supra* note 126, para. 270.

140. *Id.*

141. *Id.*

142. *Id.* at para. 274. These countries include Luxembourg, Finland,

fundamental principles of international law, transparency and reciprocity, necessitated the provision of formal notices of legal obstacles to provisional application.¹⁴³ Additionally, Claimant argued that not only had the Russian Federation given no notice of inconsistency under Article 45(1), but it had also been a firm supporter of the language creating provisional application of the ECT during ECT negotiations.¹⁴⁴

The Tribunal decided that Russia could—despite “years of stalwart and unqualified support for provisional application”—invoke the Limitation Clause to claim inconsistency between provisional application of the ECT and national laws in order to avoid provisional application of the investment protection measures of the ECT.¹⁴⁵ It based this decision on the rules of treaty interpretation found in Articles 31 and 32 of the VCLT that prevent the creation of “a notification requirement which the text does not disclose and which no recognized legal principle dictates.”¹⁴⁶ The Tribunal determined that, although the Russian Federation was subject to considerations of estoppel based on its initial support for provisional application, the conditions necessary for such a finding were not met in this case.¹⁴⁷

After concluding that Russia could rely on the Limitation Clause of 45(1) despite neither making a declaration under 45(2) nor giving prior notice under 45(1),¹⁴⁸ the Tribunal decided what effect should be given to the Limitation Clause of ECT 45(1).¹⁴⁹ The Tribunal divided this analysis into two steps:¹⁵⁰ first, whether Russia was required to provisionally apply the ECT in its entirety or whether it could be allowed to take a piecemeal approach, and second, whether the general principle of provisional application was inconsistent with

Germany, and France. *Id.*

143. *Id.* at para. 275.

144. *Id.* at para. 281.

145. *VPT Award*, *supra* note 126, para. 284.

146. *Id.* at para 283.

147. *Id.* at para. 286–88. The Tribunal found that “conditions for the existence of a situation of estoppels are not met in this case, because . . . Claimant, to succeed with its estoppels argument, would need to establish more than mere support by the Russian Federation during negotiations of the Treaty for the provisional application of the ECT.” *Id.* at para. 286.

148. *Id.* at para. 290.

149. *Id.* at para. 289.

150. *Id.* at para. 290.

Russian law.¹⁵¹

Deciding the former question, the Tribunal decided that Russia must accept an “all-or-nothing” approach to provisional application. After all, “by signing the ECT, the Russian Federation agreed that the Treaty *as a whole* would be applied provisionally pending its entry into force unless *the principle* of provisional application itself [was] inconsistent with its constitution, laws, or regulations.”¹⁵² This decision is considered “especially important . . . [for reinforcing] the binding nature of international law.”¹⁵³ Under the principle of *pacta sunt servanda*, a State would normally be prevented from using its national legislation as an excuse for a failure to perform.¹⁵⁴

The Tribunal concluded that “allowing a State to modulate (or, as the case may be, eliminate) the obligation of provisional application, depending on the content of its internal law in relation to the specific provisions found in the [ECT], would undermine the principle that provisional application of a treaty creates binding obligations.”¹⁵⁵ This rationale reinforces the integrity of international law as separate from domestic law by preventing the formation of a hybrid law “in which the content of domestic law directly controls the content of an international legal obligation.”¹⁵⁶

Having decided that provisional application would, if applied at all, be applied in its entirety, the Tribunal turned its focus to whether the principle of provisional application conflicted with Russian law.¹⁵⁷ Claimants argued that the relevant Russian law allows “an international treaty or a part thereof . . . prior to its entry into force, [to] be applied in the Russian Federation provisionally if the treaty so provides”¹⁵⁸ Further, at the time of the arbitration, Russia was subject to the provisional application of forty-five other treaties.¹⁵⁹

151. VPT Award, *supra* note 126, paras. 290, 330, 346.

152. *Id.* at para. 301 (internal citations omitted).

153. Giorgetti, *supra* note 125.

154. *Id.*

155. VPT Award, *supra* note 126, para. 314.

156. *Id.* at para. 315.

157. *Id.* at para. 330.

158. *Id.* at para. 332 (internal citations omitted).

159. *Id.* at para. 337.

In summary, the Tribunal's decision regarding provisional application of the ECT began by determining that the "regimes of provisional application in Article 45(1) and 45(2) are separate, and the Russian Federation can benefit from the Limitation Clause in Article 45(1) even though it made no declaration under 45(2)."¹⁶⁰ Next, the Tribunal found that Russia could invoke the Limitation Clause despite neither making a prior declaration nor giving any prior notice to other signatory states that it intended to use Article 45(1) to prevent provisional application.¹⁶¹ The Tribunal then noted that the Limitation Clause in 45(1) negated provisional application of the ECT only if the principle of general provisional application of the entire treaty conflicted with the constitution, laws, or regulations of the signatory.¹⁶² Finally, the Tribunal determined that no such conflict existed between the laws of the Russian Federation and the principle of provisional application of treaties.¹⁶³ Based on these conclusions, the Tribunal determined that the Russian Federation was subject to provisional application of the entire ECT until October 19, 2009, and of Parts III and V until October 19, 2029 for any investments made prior to the date of termination of provisional application.¹⁶⁴ The Tribunal asserted this decision as the basis for its jurisdiction over the arbitration, and finally concluded that Russia would be precluded from making arguments based on the inapplicability of certain ECT provisions.¹⁶⁵

II. IDENTIFICATION OF THE PROBLEM

The Yukos Tribunal confronted the issue of whether the ECT should be provisionally applied when a signatory country had made no previous declaration that provisional application was at odds with the laws of the country.¹⁶⁶ The Tribunal decided that non-declaration did not automatically mandate provisional application, but also found that Russia's national laws were not opposed to provisional application and

160. *Id.* at para. 394.

161. *Id.*

162. *Id.*

163. *Id.*

164. *Id.* at para. 395.

165. *Id.* at para. 397–98.

166. *See supra* Part I.D.

therefore Russia was obligated to comport with the terms of the treaty until its withdrawal as a signatory state.¹⁶⁷ The Tribunal's decision holding Russia to the terms of a treaty that it never fully approved raises the issue of whether provisional application is appropriate with regards to the Energy Charter Treaty and international treaty law generally, and Russia's treatment of foreign investors specifically. Provisional application of a treaty that has not yet been fully ratified is a controversial legal maneuver because it enforces treaty obligations prior to final state approval.¹⁶⁸ Because of its relative infancy in the world of customary international law, the scope and duration of provisional application, as well as the validity of the theory as a whole, needs further clarification.

III. ANALYSIS OF THE TRIBUNAL'S PROVISIONAL APPLICATION DECISION

The Tribunal's decision that the ECT should be applied as a whole to investments made in Russia prior to Russia's withdrawal as an ECT signatory sets an important, though non-binding, precedent on the treatment of treaties yet to be fully ratified that contain provisional application clauses.¹⁶⁹ Though there is no mandatory accord with the precedent of past tribunals, arbitral awards often represent a summary of the current legal thinking and state of the law. Therefore, the "outcome of the Yukos Arbitration has the potential to directly impact not only future arbitration under the ECT but, more broadly, the status, characterization, and obligations imposed by the provisional application in international law."¹⁷⁰ It has been noted that, "it will take

167. *Id.*

168. Niebruegge, *supra* note 4, at 370.

169. *Id.* at 371-72 (noting that "the Statute of the International Court of Justice does not expressly enumerate private arbitral decisions as a recognized source of international law). Furthermore, Article 32(2) of the UNCITRAL Arbitration Rules expressly denies an award precedential value by only providing that an award is "binding on the parties." *Id.*

170. *Id.* at 372. *See also* AES Corp. v. Argentine Republic, ICSID Case No. ARB/02/17, Award on Jurisdiction (2005) (*cited in* Markus Esley, "The Curious Case of the 15 Professors - Claims Against Russia Under the Energy Charter Treaty," *The Arbitrator: International Disputes Newswire* (April 2010), available at http://www.chadbourne.com/files/Publication/00012511-8e60-469a-ae3d-f2a42b6f429f/Presentation/PublicationAttachment/0dcd6d93-ba64-45e7-a224-f91bb3654518/CP_ArbitratorNews-0410.pdf (noting that "tribunals do, undoubtedly, read

quite a lot of persuasive argument to get other tribunals . . . to depart from the decision in the Yukos awards.”¹⁷¹

As noted by the Tribunal itself, the Award reinforces the doctrine of *pacta sunt servanda*, the theory that states must abide by their agreements, and of the concept that conflict with national law is not an excuse for failure to abide by the terms of an international agreement entered into force.¹⁷² Though the Tribunal did stretch this definition of *pacta sunt servanda* by placing obligations on Russia based on a treaty not yet entered into force, the Award serves as a notice that countries should not idly enter into multilateral agreements through which large investments will be made.¹⁷³ By preventing Russia from choosing which parts of the ECT to apply provisionally, the Tribunal reinforced the idea that provisional application of a treaty creates legally-binding obligations.¹⁷⁴ If the Tribunal had allowed Russia to escape the obligations imposed by provisional application, Russia would receive the benefits of investments made in reliance on the expectation of the ECT’s protection without having to afford any such protection to these investments.¹⁷⁵

The Tribunal’s decision fortifies that of the tribunal in *Kardassopoulos*, where the arbitrators found that the ECT should be provisionally applicable as a whole;¹⁷⁶ they believed that “provisional application imports the application of all the treaty’s provisions as if they were already in force, even though the treaty’s definitive entry into force had not yet occurred.”¹⁷⁷ The counsel for Kardassopoulos commented that the Yukos decision “underscores the effectiveness of provisional application as a device for giving international

prior awards on similar issues and will not disregard them lightly”).

171. Esley, *supra* note 170, at 5.

172. VPT Award, *supra* note 126, para. 312–15; *see also* VCLT, *supra* note 32, art. 26 and 27.

173. Giorgetti, *supra* note 125.

174. VPT Award, *supra* note 126, para. 316.

175. *Id.* at para. 313.

176. Kardassopoulos v. Georgia, ICSID Case No. ARB/05/18, Decision on Jurisdiction, ¶ 228 (July 6, 2007).

177. Hober, *supra* note 19, at 185. The author notes that if ‘entry into force’ in Article 1(6) of the ECT (the provision regarding the nature of investments) were construed strictly and “[meant] only definitive entry into force, it would mean that investments during the period of provisional application would be excluded from the ECT. Such a result would strike at the heart of the clearly intended provisional application regime.” *Id.*

treaties immediate and binding effect and confirms that it is in no way a watered-down application of the treaty or an aspirational exercise.¹⁷⁸

In addition to enforcing Russia's compliance with the provisions of a treaty that it had provisionally ratified, the Yukos tribunal also decreased the risk of defection by other countries.¹⁷⁹ Because the tribunal portrayed Russia's obligations as binding, affirmative, and not limited in scope,¹⁸⁰ there is no incentive for more countries in the provisional ratification stage to defer from final entry into force.¹⁸¹ Beyond specifically deterring other countries from abrogation of their treaty duties, the Yukos decision will also serve as a foundation for the future discussion of provisional application in international law.¹⁸² Because global multilateral investment treaties are on the rise, provisional application could be a key way of achieving investment protection prior to the lengthy process of full ratification.¹⁸³

The decision also has strong implications for investors in the energy sector who can claim the protection of the ECT. By holding a major energy-producing country like Russia to the terms of the ECT, the tribunal reinforced the rule of law and ended Russia's attempts to portray the ECT as an ineffective legal instrument in need of replacement; rather, the ECT has become an effective multilateral agreement to protect investors in the field of energy.¹⁸⁴ Though, as with most arbitration decisions, there is little possibility of any monetary collection by the claimants due to the bias of national court systems tasked with enforcing decisions,¹⁸⁵ collection of a possible award seems more likely in this case given the ECT's allowance of attachment of extraterritorial assets to satisfy arbitral decisions.¹⁸⁶ The Yukos decision and

178. Ross, *supra* note 121, at 11 (internal citations omitted).

179. *Id.*

180. The obligations that the Tribunal places on Russia are naturally limited to the investment protection provisions of the ECT. *See supra* Part I.D.

181. Niebruegge, *supra* note 4, at 374.

182. *Id.* at 375.

183. *Id.*

184. Alan Riley, *The EU-Russia Energy Relationship: Will the Yukos Decision Trigger a Fundamental Reassessment in Moscow?*, 2 INT'L ENERGY L. REV. 36, 37 (2010).

185. *See* Golobolov and Tanega, *supra* note 106, at 647.

186. Riley, *supra* note 184, at 37; *see also* Franz Sedelmayer v. Russian Federation, IIC 106 (1998) (allowing an arbitral decision against Russia to be

its application of the investment protection terms of the ECT furthers the purpose of the ECT—promoting and insulating investments in the energy sector.¹⁸⁷

Russia's withdrawal as a signatory of the ECT, and the Yukos tribunal's subsequent decision that Russia will be bound by the investment protection sections of the ECT for the next twenty years, possibly places on Russia the burden of affording protection to past investors without the accompanying influx of new investments.¹⁸⁸ This comes at a particularly bad time for the Russian energy sector as analysts have predicted nearly half a trillion dollars of energy-related investments as necessary by 2020 to sustain Russia's energy-producing infrastructure.¹⁸⁹ In sum, Russia will have to afford customary international law standards to investments made in its oil industry without receiving the benefits derived from an adherence to international norms, such as heightened investor confidence and lower political risk.¹⁹⁰

Some have criticized the awards for giving the protection of the ECT to an investment of foreign companies as customary under the treaty, and notably, an investment of a company primarily owned by wealthy Russians.¹⁹¹ Following this decision, Russian nationals making energy investments in Russia would be protected if they made the investment through a shell company incorporated in an alternate jurisdiction, but not if they made the investment directly.¹⁹² This may be true, but the same could be said of any multilateral or bilateral investment protection treaty that affords protection to foreigners making in-state investments.¹⁹³

Notably, applying the provisions of the treaty as a whole places a large burden on potential claimants; before bringing

enforced through the attachment of extraterritorial Russian-owned property).

187. Riley, *supra* note 184, at 37–38.

188. *Id.* at 38.

189. *Id.* (noting that internal capital cannot come close to covering the needed infrastructure investments and that Russia will therefore have to rely on international funding, a source that it cannot guarantee after the lessons that investors learned from the Yukos dispute).

190. *Id.*

191. Ross, *supra* note 121, at 12.

192. *Id.*

193. *Id.*

a case to arbitration, a prudent investor needs to ensure the entire treaty's consistency with the domestic regulations regarding provisional application of treaties, as well as the host nation's domestic laws in general.¹⁹⁴ Confusingly, this would place the burden of proof on the investor, rather than the state, to show that the treaty may be applied provisionally despite the explicit authorization of provisional application found in the text of the ECT.¹⁹⁵ The Kardassopoulos and subsequent Yukos decisions may "[reduce] investor confidence in the ECT" due to this switch of the burden of proof.¹⁹⁶ Importantly, though, the provisional application of the treaty as a whole would reduce the confidence level of investors less than the application of the treaty in part.¹⁹⁷ Provisional application imposes a large hurdle for an investor already facing years of complex arbitration, but it is the nature of complex international investment law and still in the interest of claimants to pursue.

IV. PROPOSAL

As noted in Part III, the Yukos Tribunal's decision follows the existing case law and treaty law relating to provisional application.¹⁹⁸ The issue of provisional application arises because of a lack of precision in the drafting of treaty language, sometimes purposeful and other times the result of lack of foresight.¹⁹⁹

In the aftermath of the *Kardassopoulos* decision, scholars suggested additions to the language of the ECT, specifically to Art. 45(1), that would have prevented the rise of disputes as occurred in Yukos.²⁰⁰ By reinforcing Art. 45(1) with language that clearly requires a signatory to make a declaration if provisional application is inconsistent with domestic regulations or to forego the domestic law defense to

194. Piotr Szvedo, Case Comment: (*Former*) *Yukos v. Russian Federation before the Permanent Court of Arbitration*, 18 J. INT'L COOPERATION STUDIES 57, 62 (2010).

195. Belz, *supra* note 28, at 745.

196. *Id.*

197. Szvedo, *supra* note 194, at 62.

198. *See supra* Part III.

199. Belz, *supra* note 28, at 755.

200. *See, e.g., id.*

provisional application,²⁰¹ the preliminary debate addressed by the Interim Yukos Award would not have been needed as the language of the treaty would have provided a clear answer.

The ECT would also benefit from a clearer delineation of the duration of provisional application for countries like Belarus and Russia (prior to its withdrawal), which have signed but not ratified the ECT.²⁰² In the aftermath of the *Kardassopoulos* decision, scholars proposed such language, and if this language had been present in the ECT at the time of the Yukos dispute, a substantial portion of the Tribunal's decision would have been unnecessary.²⁰³ This language would resolve the indefiniteness of the ECT's provisional application clauses and would "encourage states to either ratify or express their intent not to be bound by the treaty,"²⁰⁴ the very problem that stimulated the Yukos dispute between ECT investors and Russia.

A redraft of the treaty or amendments to its provisional application sections would give investors and host states a clearer picture of what is expected under the ECT's use of provisional application. Those changes would also guide future tribunals on the intent of the treaty's drafters.²⁰⁵

CONCLUSION

The Tribunal's decision is well-reasoned and supported by detailed scholarship. Its conclusion that Russia must provisionally apply the ECT's investor protection provisions is

201. See *id.* at 755–56 (suggesting that Article 45(1) be amended with the language: "If provisional application is inconsistent with a signatory's constitution, laws, or regulations, that signatory must make a declaration upon signature rejecting provisional application pursuant to paragraph 2(a). If the signatory fails to make this declaration upon signature, the signatory thereafter waives its rights to assert that provisional application is inconsistent with its constitution, laws, or regulations.").

202. *Id.* at 759.

203. *Id.* (suggesting that an additional clause be added to Art. 45 with the language: "If after ___ years following the Treaty's definitive entry into force a signatory provisionally applying the Treaty has not expressed its consent to be bound by the Treaty through ratification, acceptance, or approval, or voluntarily terminated its provisional application of the Treaty pursuant to Article ___, the signatory's provisional application of the Treaty will terminate.").

204. *Id.*

205. It is worth noting that it would be difficult to reach an agreement and possibly not worth the effort. Before renegotiation began, the parties should examine the costs and potential benefits of clarification of the treaty's terms.

in close accord with the plain text on provisional application in the treaty.²⁰⁶

Regardless of the results of the merits phase of the arbitration, investors are more likely to focus on the political risk of investing in Russia after its treatment of Yukos and its subsequent withdrawal from the ECT.²⁰⁷ Even though the Yukos Tribunal afforded protection to prior investments continuing long after Russia's withdrawal, it cannot extend this protection to new investments made in Russia after the withdrawal.²⁰⁸ Despite the risky climate for foreign investment in Russia's energy sector, there are many opportunities for investment.²⁰⁹ To avoid future disputes related to multilateral investment treaties, treaties should be updated to address in detail the scope and limitations of provisional application.²¹⁰

The Tribunal's Interim Award signals that Russia is no longer immune from the effects of the investment protection treaties it has signed.²¹¹ Allowing the Tribunal to move forward to the merits phase is an important step towards fairness in Russian investment disputes, and the release of the decision is a move towards transparency in Russian dispute settlements.²¹² However, despite an initial victory for the claimants, "it is already clear that complete victory for either the former Yukos owners or the Russian Federation is unlikely"²¹³ because of the high cost of complex arbitration,

206. Giorgetti, *supra* note 125 (citing OPPENHEIM'S INTERNATIONAL LAW 1238 (Sir Robert Jennings and Sir Arthur Watts eds., 9th ed. 1992) (noting that affirmation of a treaty may mandate provisional application)).

207. Riley, *supra* note 184, at 38. See also Daniel R. Sieck, Note, *Confronting the Obsolescing Bargain: Transacting around Political Risk in Developing and Transitioning Economies through Renewable Energy Foreign Direct Investment*, 33 SUFFOLK TRANSNAT'L L. REV. 319, 321-323 (2010) ("Political risk is an ever-present danger of [foreign direct investment] that is especially profound in the energy sector When investors operate in foreign legal regimes, they face an increased level of general business risk uncommon in domestic ventures.").

208. See *supra* Part I.

209. Waltrip, *supra* note 1, at 586 (noting that capacity and technology updates needed by Russia will cost at least fifty billion dollars over the next ten years, and that the Russian Ministry of Natural Resources plans to encourage development of new oil fields and the creation of tax breaks for new exploration in encouragement of further development).

210. See Belz, *supra* note 28, at 759.

211. Rubins and Nazarov, *supra* note 57, at 113.

212. Niebruegge, *supra* note 4, at 375.

213. Golobolov and Tangege, *supra* note 106, at 647.

the small possibility of collecting a judgment from Russia, and the public relations disaster that has occurred for all parties.²¹⁴

Before the Tribunal's decision in 2006, the Secretary General of the Energy Charter Secretariat, Andre Mernier, lamented the uncertainty of "the extent to which provisional application of the [ECT] creates firm legal rights and obligations for Russia . . . under international law."²¹⁵ The Yukos Tribunal clarified a great deal of that uncertainty, while the Yukos Interim Award will serve as a strong foundation for holding host nations accountable for protection of investments made during provisional application of the ECT; however, the addition of new, clear language with respect to provisional application would be the best foundation for preventing future disputes.

214. *Id.* The tribunal has attracted much attention in the media, both for the exposure of what seems to be a Russian coup of the foreign energy infrastructure, and for the immense monetary amount of the claimants' demand. See Ross, *supra* note 121, at 11.

215. Andre Mernier, Sec'y Gen., Energy Charter Secretariat, Speech to the International Conference on Energy Security: the Energy Charter and International Energy Security, Moscow (Mar. 14, 2006), available at http://www.encharter.org/index.php?id=59&id_article=75&L=0 (cited in Belz, *supra* note 28, at 729).