School of International Arbitration, Queen Mary, University of London

International Arbitration Case Law

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"The following is a preliminary version of the IACL summary on this decision. This summary has not yet undergone review by a member of the IACL editorial committee. The final summary along with translations to Spanish and French will be posted early this fall."

GEA GROUP AKTIENGESELLSCHAFT
V. UKRAINE
(ICSID CASE NO. ARB/08/16

Case Report by Ileana M. Smeureanu and Lucia Druetta**
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On 31 March 2011, an Award was made under the ICSID Convention and the 1993 Agreement between the Federal Republic of Germany and Ukraine ("BIT") dismissing all GEA's ("Claimant") claims and holding it responsible for all reasonable costs incurred by Ukraine ("Respondent") in defending its case before the ICSID Tribunal.

Tribunal:	Prof. Albert Jan van den Berg (President), Mr. Toby Landau, Prof. Brigitte Stern
Claimant's Counsel:	Mr. Barton Legum, Ms. Brenda Horrigan, Ms. Anne-Sophie Dufêtre and Mr. Gaunthier Vannieuwenhuysse, SCP SALANS & ASSOCIES (FRANCE); Mr. George Burn, SALANS LLP (UK)
Defendant's Counsel:	Mr. Sebastian Seelmann-Eggebert and Mr. Jan Erik Spangenberg, LATHAM & WATKINS LLP (GERMANY); Mr. Robert Volterra, Mr. Charles Claypoole, Ms. Hussein Haeri and Ms. Michelle Bradfield, LATHAM & WATKINS (UK);

	Mr. Serhii Sviriba and Mr. Dmytro Marchukov, Magisters (UKRAINE)

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1. Facts of the Case

The dispute arose from Claimant's alleged investment in Ukraine in form of capital loans to a former state-owned entity called OJSC Oriana ("Oriana"). In 1995, Oriana, an Ukrainian *kombinat*, concluded a contract with a member of the German Klöckner group, Klöckner & Co Handel Aktiengesellschaft ("Klöckner"). Under the contract, Klöckner undertook to provide Oriana with 200,000 tons of naphtha fuel for conversion on a yearly basis (the "Conversion Contract").

Between 1996 and 1998, Oriana entered into 147 (out of a total of 154) amendments to the Conversion Contract with Klöckner Chemiehandel GmBH ("KCH"), a company that dealt with the chemical business of the Klöckner group. In 1997, MG Technologies AG, GEA Group Aktiengesellschaft's predecessor, acquired all shares in KCH though a wholly-owned subsidiary. KCH subsequently changed its name and merged into Solvadis Chemag AG. On 28 June 2004, Solvadis Chemag (formerly KCH) assigned all its rights connected with its business with Oriana and all its rights in the underlying transactions to MG Technologies AG. In 2005, MG Technologies AG changed its name into GEA Group Aktiengesellschaft ("GEA").[1]

The relation between Oriana and Klöckner started to deteriorate in December 1997, when a person responsible to periodically inspect Oriana's work (Dr. Chperoun) was shot in the kneecap. Shortly thereafter, many discrepancies between the quantity of raw materials shipped to Oriana and the quantity of finished products were discovered. According to a July 2008 audit report, more than 125,000 metric tones of finished products (the "Products") were missing.[2]

Following these incidents, KCH/Klöckner, Oriana and representatives of the Ukrainian Government engaged in a series of discussions regarding the alleged misappropriation. As a result thereof, on 7 August 1998, Oriana and KCH concluded a settlement agreement under which Oriana acknowledged its indebtedness to KCH for the value of the products that should have been delivered under the Conversion Contract and those actually delivered or available for delivery (the "Settlement Agreement"). All disputes under the Settlement Agreement were to be resolved through ICC arbitration. On 29 September 1998, Oriana and KCH entered into a Repayment Agreement under which Oriana agreed to pay KCH "at least USD 27.6 million", part of which accounted for the

[1] Award ¶¶ 38-40, 46.

[2] Award ¶¶ 46-47.

undelivered products. The Repayment Agreement also provided for ICC arbitration and was signed for Oriana by three individuals (Messrs Sljuzar, Gabel and Haber) whose authority to represent it was disputed in the proceedings to follow.[3]

Following its 1998 bankruptcy and subsequent reorganization, Oriana was unable to perform its obligations under the Repayment Agreement. Consequently, in 2001, KCH (renamed Solvadis International) initiated an ICC arbitration against it. The ensuing award was largely in favor of Solvadis International, granting it USD 30,381,661.44 as primary compensation, 3% interest per annum from 28 December 2000, USD 273,000 in arbitration costs, and EUR 141,689.38 in legal fees and expenses.[4] Solvadis International unsuccessfully tried to enforce the award in Ukraine for several years. The local courts rejected its applications on the grounds that the Repayment Agreement was invalid as it had been concluded by unauthorized persons.[5]

While enforcement proceedings were pending, Solvadis International also ineffectively tried to claim under the ICC award in bankruptcy proceedings against Oriana. The bankruptcy claims were dismissed as time-barred. Solvadis's argument that the ICC award confirmed Oriana's indebtedness was rejected on the grounds that the award had not been recognized and enforced by Ukrainian courts.[6] Following these events, in 2008, GEA (formerly Solvadis International), filed a Request for ICSID arbitration under Art. 13(2) of the 1993 Agreement between the Federal Republic of Germany and Ukraine on the Promotion and Mutual Protection of Investments (the "BIT"). The ICSID Tribunal issued an award on 31 March 2011.

2. Legal Issues Discussed in the Decision

2.1 Jurisdiction

In order to determine its jurisdiction over the dispute, the Tribunal analyzed whether (1) GEA had standing to bring the arbitration claims, (2) whether GEA made an investment in Ukraine, and (3) whether the Ukraine's alleged BIT violations occurred before the alleged investment.

(a) Does GEA have standing? (¶¶ 94-125)

Respondent challenged Claimant's standing on the ground that the Conversion

[3] Award ¶¶ 49-54.
[4] Award ¶¶ 56-62.
[5] Award ¶¶ 63-67.
[6] Award ¶¶ 68, 72-84.

Contract, as the core of the alleged investment, vested not in KCH, but in Klöckner. The Tribunal rejected Respondent's argument. Despite no outright mention that KCH acquired rights from Klöckner under the Conversion Contract, the Settlement Agreement and two subsequent protocols between Respondent, Oriana and KCH's parent company recorded Oriana's indebtedness to KCH under the Conversion Contract, as well as its rights thereunder. KCH also validly entered into 147 out of a total of 154 amendments to the Conversion Contract.[7] Thus, the Tribunal concluded that the rights in the Conversion Contract undeniably vested in KCH.

Respondent also objected to Claimant's standing to raise claims after in 2004 the latter sold KCH to a private equity fund. Claimant argued in response that the sale took place around the same time with an assignment of rights by Solvadis Chemag (formerly KCH) to Claimant to pursue claims against Oriana and Respondent. Under German law, according to Claimant, this assignment entered into effect before the sale. Based on the lack of evidence supporting Claimant's position, the Tribunal determined that Claimant had standing to pursue claims only until the 2004 sale and sustained Respondent's objection.[8] The Tribunal also confirmed that a requirement of ownership or control of the investment at the time of registration of an arbitration request under the ICSID Convention did not exist under the BIT, ICSID Convention or ICSID Rules.[9]

(b) Did GEA Made an Investment? (¶¶ 126-164)

Claimant asserted that its investment in Ukraine may be comprised of: (i) the Conversion Contract and the property rights thereunder, (ii) the Settlement Agreement and the Repayment Agreement, and (iii) the ICC Award on its own.[10]

Acknowledging that the ICSID Convention contains no definition of "investment", the Tribunal referred to the criteria spelled out in the existing case law and the ICSID Convention's *travaux préparatoires* to determine whether GEA actually invested in Ukraine. "The limits of this concept [of investment] are susceptible to agreement, or a subjective definition by the State Parties in legal instruments such as BITs or National laws, which embody their consent to ICSID jurisdiction".[11] Thus, the Tribunal embraced "a more flexible and pragmatic approach … which takes into account the

[7] Award ¶¶ 101-104.
[8] Award ¶¶ 107-118.
[9] Award ¶¶ 121-125.
[10] Award ¶ 144.
[11] Award ¶ 142.

features identified in *Salini*, but along with all circumstances of the case, including the nature of the instrument containing the relevant consent to ICSID".[12]

In light of "all potentially applicable criteria",[13] the Tribunal held that the Conversion Contract and the Products were an investment within the meaning of the BIT and the ICSID Convention. The Contract met the requirements of Art. 1(1)(e) of the BIT in that it conferred the right for GEA, through KCH, to "exercise an economic activity" in Ukraine, and established a "common interest" through KCH's/GEA's assistance with delivery of logistics and pay for Ukrainian domestic freight, customs issues and supply of materials to Oriana. The Conversion Contract also met the "objective definition" of investment under Art. 25 of the ICSID Convention: Claimant provided some contribution to Ukraine, during a certain period of time, while assuming the risks of economic operation during its undertaking. [14]

The Settlement Agreement, allegedly recognizing the "validity of the claims to performance" and the Repayment Agreement quantifying "the minimum value of the claims and set[ting] out a mechanism for the value of the claims to be materialized" did not "in and of themselves" constitute investments. The Settlement Agreement only contained an inventory of undelivered goods and recorded a debt by Oriana to KCH, while the Repayment Agreement only established a means of debt repayment.[15]

Finally, the Tribunal dismissed Claimant's submission that, by liquidating the amount due under the Settlement Agreement and the Repayment Agreement as of 2002, the ICC Award was an investment "in and of itself" under Art. 1(1)(c) of the ICSID Convention. The Award was neither a "contribution to, or relevant economic activity, within Ukraine" under Art. 1(1) of the BIT and Art. 25 of the ICSID Convention, nor a "change of form in which assets are invested" under Art. 1 of the BIT. Instead, the award qualified as a "legal instrument" providing for the disposition of rights and obligations arising out of the Settlement Agreement and the Repayment Agreement, neither of which was an investment.[16]

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[12] Award ¶142, citing *Biwater Gauff (Tanzania) v. Tanzania*, ICSID Case No. ARB/05/22, Award, 24 July 2008, ¶¶ 312-316.
[13] Award ¶ 143.
[14] Award ¶¶ 149-153.
[15] Award ¶¶ 154-157.
[16] Award ¶ 159-162.

(c) Did the Alleged Violations Occurred Before the Alleged Investment ? (¶¶ 165-203)

The Tribunal determined that Claimant had an interest in the Conversion Contract (i.e., the investment) between December 1997 and June 2004. It also held that it had jurisdiction over the alleged Treaty violations occurred during this period: the taking of Claimant's Products, Respondent's behavior following Dr. Chperoun's shooting, and its conduct in enforcing the ICC Award and in the bankruptcy proceedings. [17]

2.2 Liability

In light of Claimant's submissions, the Tribunal had to determine whether Respondent breached the BIT provisions related to: (a) expropriation, (b) full protection and security, (c) fair and equitable treatment, (d) arbitrary and discriminatory measures, (e) national treatment and most-favored nation treatment, and (f) adherence to obligations.

(a) Expropriation (¶¶ 207-238)

Claimant argued that the misappropriation of 125,000 metric tons of its Products from Oriana and the Ukrainian courts' failure to recognize and enforce the ICC Award amounted to expropriation under Art. 4(2) of the BIT. The Tribunal dismissed both submissions. Claimant failed prove that the misappropriation constituted an expropriation and a not a private theft. Without supporting evidence, its submissions were rejected as speculative. [18] Claimant neither demonstrated that Respondent's courts applied their laws discriminatorily in the process of recognition and enforcement, or were "egregious" in their conduct, or prevented GEA's ability to recover under the ICC Award. [19] Thus, no expropriation was committed in connection with the misappropriation of Products and the Ukrainian courts' treatment of the ICC Award.

(b) Full Protection and Security (¶¶ 239-267)

Claimant contended that Respondent failed to ensure full protection and security under Art. 4(1) of the BIT by not criminally punishing the theft of Products, Dr. Chperoun's shooting and Mr. Sljuzar's unauthorized signature of the Repayment Agreement. Based on the available evidence, the Tribunal found instead that: (i) GEA itself failed to initiate criminal proceedings for the taking of Products,[20] (ii) the shooting had been investigated

[17] Award ¶¶ 165-203
[18] Award ¶¶ 211-226.
[19] Award ¶¶ 227-237.
[20] Award ¶¶ 246-249.

by Ukrainian prosecutors but remained unresolved,[21] and (iii) Mr. Sljuzar misrepresentation as to his status of president of Oriana did not trigger Respondent's responsibility because Oriana was an entity independent from the State when the Repayment Agreement was signed.[22] Thus, the Tribunal rejected also Respondent's submissions on this point.

(c) Fair and Equitable Treatment (¶¶ 268-324)

According to Claimant, Respondent also violated its fair and equitable obligations under Art. 2(1) of the BIT by (i) not honoring its promise to compensate GEA for the wrongfully taken property, (ii) defeating GEA's expectations to recover Oriana's debt during the bankruptcy proceedings, and (iii) by not supporting GEA's effort to enforce the ICC Award before Ukrainian courts. As to Claimant's first submission, the evidence did not indicate whether Respondent ever made or failed to comply with any repayment promise.[23] The record neither showed that Respondent promised Claimant to terminate the bankruptcy proceedings against Oriana, nor that it granted custody over Oriana's assets in violation of Ukrainian law, or that Respondent deliberately transferred some of Oriana's assets to a newly created joint venture to avoid liability.[24] Finally, the Tribunal analyzed under the *Mondev* test[25] whether Respondent's failure to recognize and enforce the ICC Award led to "justified concerns as to the judicial propriety of the outcome … having regard to generally accepted standards of the administration of justice".[26] After examining the decisions of the Ukrainian courts, the Tribunal determined that the refusal of recognition and enforcement arose not as a matter of abusive practice, but only after the courts heard Claimant's arguments and dismissed them.[27] There were therefore no grounds to hold Respondent accountable for any violation of fair and equitable treatment.

(d) Arbitrary and Discriminatory Measures (¶¶ 325-331)

Claimant further claimed that Respondent's alleged misappropriation of 125,000 metric tones and its constant obstruction to GEA's residual interest in Oriana infringed its BIT obligations of not "impair[ing] by arbitrary of discriminatory measures the

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[21] Award ¶¶ 253-255.
[22] Award ¶¶ 262-266.
[23] Award ¶¶ 277-283.
[24] Award ¶¶ 286-305.
[25] Mondev International Ltd. v. United States of America, ICSID Case No. ARB(AF)/99/2, Award, 11 October 2002, ¶ 127.
[26] Award ¶¶ 312 citing Mondev, *supra* note 19.
[27] Award ¶¶ 315-319.

management, maintenance, use or enjoyment of investments … within its territory".[28] Noting that Claimant raised the same grounds for its fair and equitable treatment claims, the Tribunal rejected Claimant's latter submissions for the same reasons it dismissed the former.[29]

(e) National Treatment and Most-Favored Nation Treatment (¶¶ 332-345)

Claimant also advanced several discrimination claims in connection with (i) its claim's rejection as time-barred in Oriana's bankruptcy in contrast with the recognition of a simultaneous claim advanced by another foreign company, (ii) the non-enforcement of the ICC Award on grounds that the Repayment Agreement had been invalidly signed while other contracts signed under allegedly similar circumstances were apparently held effective, and (iii) a provision in the Ukrainian Law on Foreign Economic Activity supposedly imposing more burdensome contract signature requirements on foreign than on national investors.[30] Based on the record, Claimant's first two submissions were dismissed for contradicting and lack of evidence, respectively. As to the third claim, the Tribunal acknowledged that the law created additional investment requirements for foreigners, but pointed that they did not affect the treatment of investments once made. Accordingly, Claimant's discrimination submissions were rejected.[31]

(f) Adherence to Obligations (¶¶ 346-356)

Lastly, Claimant argued that, by not honoring its alleged promise to compensate GEA for the appropriated property, Respondent breached its adherence obligations assumed "with regard to investments of nationals or companies of the other Contracting States in its territory".[32] The record, however, showed that Respondent's conduct was at best "an indication" of best efforts rather than a promise for anything towards GEA.[33] Consequently, Respondent did not violate any of its "other obligations" under the BIT.

(g) Damages and Costs (¶¶ 357-366)

Since Respondent was not found liable under any count, the Tribunal did not address Claimant's damages claims. In deciding the costs, the Tribunal applied Art. 61(2) of the ICSID Convention in Respondent's favor and held Claimant responsible for the

[28] Award ¶ 325 citing Art. 2(3) of the BIT.
[29] Award ¶¶ 329-331.
[30] Award ¶¶ 333-336.
[31] Award ¶¶ 341-345.
[32] Award ¶ 346 citing Art. 8(2) of the BIT.
[33] Award ¶¶ 351-356.

former's "reasonable costs". Accordingly, Claimant was ordered to reimburse Respondent all of its costs totaling USD 1,595,337.47 and UAH 4,300.[34]

3. Decision

The Tribunal rejected all Claimant's claims within its jurisdiction and ordered it to pay Respondent's costs.

[34] Award ¶¶ 357-366.