

Swiss Supreme Court dismisses challenges to interim awards on jurisdiction rendered in investor-state arbitrations

by Prof. Dr. Nathalie Voser (Partner), *Schellenberg Wittmer Ltd*

Legal update: case report | [Published on 28-Nov-2018](#) | International, Switzerland

In decisions *4A_396/2017* and *4A_398/2017*, the Swiss Supreme Court considered requests to set aside two interim awards on jurisdiction rendered in treaty based investor-state arbitrations which were brought on the basis that the arbitral tribunal had wrongfully accepted jurisdiction.

Speedread

In two decisions dated 16 October 2018, and published on 16 November 2018, the Swiss Supreme Court declined the Russian Federation's requests to set aside two interim awards for lack of jurisdiction.

The Supreme Court found that the arbitral tribunal rightly held, that the territorial scope of the bilateral investment treaty between the Russian Federation and the Ukraine of 27 November 1998 (Russia-Ukraine BIT), includes the Crimea as a territory over which the Russian Federation exercises de facto control. With respect to the subject-matter scope of the Russia-Ukraine BIT, the court concluded that the term "investment" in Article 1(1) of the Russia-Ukraine BIT also comprises investments originally made in the investor's home state that are only subsequently located in the host state as a result of a shift of borders. (*Decisions 4A_396/2017 and 4A_398/2017, (dated 16 October 2018, and published on 16 November 2018).*)

Background

Article 190(2)(b) of the Private International Law Act provides that an award will be set aside if the arbitral tribunal wrongfully accepted or declined jurisdiction.

Article 29 of the *Vienna Convention on the Law of Treaties 1969* (VCLT), provides that a contracting state is bound by an agreement "with respect to its entire territory" unless a different interpretation appears from the treaty or is otherwise established.

Article 1(1) of the Russia-Ukraine bilateral investment treaty (BIT) defines investments in a non-exhaustive list of assets and provides in relevant part:

"The term 'investments' means any kind of tangible and intangible assets [which are] invested by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's legislation..."

It further provides that "[a]ny alteration of the type of investments in which the assets are invested shall affect their nature as investments, provided that such alteration is not contrary to legislation of a Contracting Party in the territory of which the investments were made".

Article 2(1) of the Russia-Ukraine BIT provides:

"Each Contracting Party will encourage the investors of the other Contracting Party to make investments in its territory and admit in accordance with its legislation."

Article 2(2) of the Russia-Ukraine BIT provides:

"Each Contracting Party guarantees, in accordance with its legislation, the full and unconditional legal protection of investments by investors of the other Contracting Party."

Article 12 of the Russia-Ukraine BIT provides that it "shall apply to all investments made by investors of one Contracting Party in the territory of the other Contracting Party on or after January 1, 1992".

For further information on the definition of investments in investment treaty arbitration, see *Practice note, Definition of investment in international investment law*.

Facts

In 2015, several Ukrainian entities initiated two investor-state ad hoc arbitrations under the UNCITRAL Arbitration Rules against the Russian Federation under Article 9 of the Russia-Ukraine BIT. The Ukrainian entities alleged that their assets in the Crimean Peninsula were expropriated after the incorporation of the Crimea into the Russian Federation in March 2014. The arbitrations, administered by the Permanent Court of Arbitration, were seated in Switzerland.

By letter from its Ministry of Justice dated 12 August 2015, and a letter from its Ambassador to the Netherlands dated 15 September 2015, the Russian Federation contested the jurisdiction of the arbitral tribunal with respect to the claims asserted in both arbitrations. The Russian Federation did not further participate in the arbitration proceedings.

In June 2017, the arbitral tribunal rendered two interim awards affirming its jurisdiction. The Russian Federation challenged these awards before the Swiss Supreme Court, arguing that the arbitral tribunal lacked territorial, personal and subject-matter jurisdiction.

Decision

The Swiss Supreme Court ultimately rejected the set-aside applications, dismissing the argument that the arbitral tribunal had wrongly accepted jurisdiction.

At the outset, the Supreme Court confirmed that its power of judicial review is unlimited even when reviewing interim awards on jurisdiction in investment arbitration proceedings.

With respect to the territorial scope of the Russia-Ukraine BIT, the Supreme Court noted that there was no need to comment on the legality of the incorporation of the Crimea into the Russian Federation under international law as the Russian Federation did not dispute that the territory of the Russia-Ukraine BIT also comprises territory that is only de facto controlled.

The court found that the arbitral tribunal had properly interpreted the term "territory" in Article 1(4) of the Russia-Ukraine BIT in accordance with general principles of international law. In this respect, the Supreme Court referred to Article 29 of the VCLT, and stated that it is decisive that a treaty is still applicable to its entire territory in case of territorial changes. Further, the Supreme Court found that a change of borders does not require a subsequent agreement between the contracting parties pursuant to Article 39 of the VCLT or Article 13 of the Russia-Ukraine BIT. The Supreme Court concluded that the arbitral tribunal rightly held that the territorial scope of the Russia-Ukraine BIT includes the Crimea as a territory over which the Russian Federation exercises de facto control.

Regarding the subject-matter scope of the Russia-Ukraine BIT, the Supreme Court noted that the term "investment" needs to be interpreted pursuant to the principles of interpretation set out in Article 31 of the VCLT, including the *effet utile* (usual effect) principle. The Supreme Court found that it is not clear from the wording along of Article 1(1) of the Russia-Ukraine BIT whether it requires that the investment be a cross-border investment from the outset or whether it suffices that the investment is located in the territory of the host state only at a later point in time.

Further, the Supreme Court noted that the interpretation of the term "investment" in previous awards rendered by other tribunals under the Energy Charter Treaty to which the Russian Federation had referred, was irrelevant to the interpretation of this term in the Russia-Ukraine BIT. The Supreme Court explained that previous arbitral awards are not a "real source of law" ("*keine eigentliche Rechtsquelle*") for the arbitral tribunal and that the definition of "investment" in another treaty does not necessarily have the same meaning as in the Russia-Ukraine BIT.

The Russian Federation had asserted that the term "investment" under Article 1(1) of the Russia-Ukraine BIT required an act of a cross-border investment at a certain point in time. However, the Supreme Court found that the use of the term "invest" in other provisions of the Russia-Ukraine BIT militates against a temporal restriction in the sense that only investments that are cross-border at the time of inception are comprised. While Article 1(1) of the Russia-Ukraine BIT uses an imperfective aspect in the Russian and Ukrainian authentic versions, Article 12 of the Russia-Ukraine BIT uses a perfective aspect. In the Supreme Court's view, the perfective aspect denotes a specific point in time, whereas the imperfective aspect indicates a continuous action. The element of duration can, in the Supreme Court's view, also be found indirectly at the end of Article 1(1) of the Russia-Ukraine BIT, according to which a subsequent alteration of the type of investment does not affect its nature as an investment.

In addition, the Supreme Court found that Article 1(1) of the Russia-Ukraine BIT, which contains a non-exhaustive list of assets qualifying as investments is an "asset"-based definition of investment in contrast to a "transaction"-based definition. A "transaction"-based definition mainly reflects earlier thinking on the liberalisation of capital movements and ignores the aspect of investment protection of assets and rights which are not directly related to a cross-border transaction. The requirement in Article 1(1) of the Russia-Ukraine BIT that the investment was made in accordance with the law of the host state is inherent in the system. This requirement is not decisive for the question of impact of a shift of borders with regard to investments.

In the Supreme Court's view, the arbitral tribunal's interpretation of the term "investment" in the Russia-Ukraine BIT does not contradict the object and purpose of the Russia-Ukraine BIT. The title and preamble of the Russia-Ukraine BIT aim at promoting and protecting investments. In a similar vein, Article 2 of the Russia-Ukraine BIT

aims at protecting investments. The Russian Federation did not, in the Supreme Court's view, successfully rebut the arbitral tribunal's finding that the Russia-Ukraine BIT has a dual purpose. In the court's finding, Article 12 of the Russia-Ukraine BIT confirms, that the protection of investments is a separate and independent purpose from the encouragement of investments since this provision also protects investments that were made between 1 January 1992, before the entry into force of the Russia-Ukraine BIT, and 2000 and could therefore not be considered as having been promoted by the BIT. In addition, the court stated that the relevant point in time to determine whether the investment constitutes an investment in the host state within the meaning of Article 1(1) of the Russia-Ukraine BIT, is the time of the act of infringement as the host state shall not be able to frustrate investments of investors of the home state without consequences.

The Supreme Court further found that a systematic interpretation of the Russia-Ukraine BIT does not lead to a more restrictive interpretation of the term "investment". In the court's view, the arbitral tribunal correctly interpreted Article 12 of the Russia-Ukraine BIT, which governs the temporal scope of the Russia-Ukraine BIT. Similarly, according to the court the definition of investor in Article 1(2) of the Russia-Ukraine BIT as well as Articles 2(1) and 2(2) of the Russia-Ukraine BIT do not support the Russian Federation's narrow interpretation of Article 1(1) of the Russia-Ukraine BIT.

Comment

On 16 October 2018, the Supreme Court held a public deliberation as there was disagreement between the three justices of the chamber who formed the initial bench that considered both cases. At the public deliberation, which is very rare in setting-aside proceedings, one of the five Supreme Court's judges submitted her dissenting opinion. Two further Supreme Court judges stated that they had reservations but eventually agreed with the majority position. Therefore, the judgment was ultimately rendered by a majority.

According to the dissenting judge, the arbitral tribunal had wrongly assumed jurisdiction. She stated that the definition of "investment" in Article 1(1) of the Russia-Ukraine BIT does not cover any and all investments as this provision does not contain an unlimited or unqualified definition of investment. Rather, Article 1(1) of the Russia-Ukraine BIT requires that an investor of one state invests in the territory of the other state. This, in her view, includes the transaction by which the investment is made. She concluded that the Russia-Ukraine BIT does not follow an asset-based approach, and thus as asset-based definition of definition as many modern BITs, but rather a transaction-based definition.

In the dissenting judge's view, the systematic interpretation of the Russia-Ukraine BIT does not lead to a different result. In particular, Article 12 of the Russia-Ukraine BIT confirms the need for a cross-border investment from the outset. This provision does not support the understanding whereby domestic investments that only later become foreign investments are also covered by the Russia-Ukraine BIT. If in fact only the time of the alleged violation of the BIT was relevant to assess whether the investment qualified for protection, there would be no need for any temporal limitation such as the one provided for in Article 12 of the Russia-Ukraine BIT.

In addition, the dissenting judge stated that the object and purpose of the Russia-Ukraine BIT confirm her understanding of the meaning of investment in Article 1(1) of the Russia-Ukraine BIT, namely that the purpose of the Russia-Ukraine BIT is to promote investments from one state to another state and to protect only such cross-border investments.

The dissenting judge further stated that when entering into the Russia-Ukraine BIT in 1998, the contracting parties did not contemplate that the BIT would apply to investments that were originally made in the home state of the investor and only later were located in the host state due to a shift of borders. She opined that this

constitutes a gap in the Russia-Ukraine BIT that the Supreme Court is prohibited from filling. She concluded that the other judges' interpretation of investment was an impermissible supplementation of the treaty ("*unzulässige Vertragsergänzung*").

As Schellenberg Wittmer represented the Russian Federation in the set-aside proceedings, we refrain from commenting further on the decisions.

Cases

Decision 4A_396/2017 and *Decision 4A_398/2017*, (dated 16 October 2018, and published on 16 November 2018).

END OF DOCUMENT