

## **BUSINESS IN CHECK: THE IMPACT OF INVESTMENT DISPUTES ON BELARUS'S IMAGE**

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### **Summary**

**A Ukrainian businessman and his Swiss company accuse Belarus of reneging on international obligations to protect foreign investments and claims USD175 million in compensation. Belarus has never before acted as a respondent in an investment dispute. Previously, disputes in Belarus arose between foreign investors and specific state-controlled enterprises and never reached the state level.**

### **An investor vs. the state**

According to a report by the International Center for Settlement of Investment Disputes (ICSID, Washington), [it became known on 17 September 2013](#) that Gennady Mykhailenko, a Ukrainian national, filed a notice of dispute seeking to bring an ICSID claim for USD175 million over the expropriation of his investment in a seamless steel pipe factory (PUIP Upeco Industries) in the Republic of Belarus. At the moment the ICSID Secretariat considers accepting Mykhailenko's claim and determines whether the application complies with formal requirements.

Gennady Mykhailenko and a Swiss company he co-owns, United Pipe Export Company Trading AG, filed a request to consider the lawfulness of their claims associated with the breach by the Republic of Belarus of the bilateral agreements on protection of investments with Ukraine and Switzerland. These agreements create a liability of the state for unlawful expropriation of an investor's property. Mykhailenko is represented by a team from Paris boutique [Lazareff Le Bars](#) consisting of managing partner Benoit Le Bars and senior associate Romilly Holland. There are no reports that Belarus has instructed external counsel.

### **How the ICSID accepts requests for arbitration**

The [International Centre for Settlement of Investment Disputes](#) is an international arbitration institution which facilitates arbitration and conciliation of legal disputes between states and international investors. The organization has more than 149 members, including Belarus, which signed and ratified the ICSID Convention on the Settlement of Investment Disputes in 1992. The ICSID was established to promote the flow of foreign private capital in third countries. The signing of the Convention does not mean that the contracting party automatically falls under the ICSID jurisdiction. In order for the ICSID to accept a request for conciliation/arbitration, it has to pass initial review for compliance with formal requirements. A review can be filed with the ICSID based upon the following grounds:

- A written agreement between the parties (for instance, an investment agreement between the state and the investor), in which the parties designate the ICSID as the place of arbitration;
- A relevant provision in the intergovernmental bilateral agreement on the mutual protection of investments (for fairness' sake, we should point out that neither the Belarus-Ukraine Bilateral Investment Treaty (BIT), nor the Belarus-Switzerland BIT directly designate the ICSID as the place of arbitration for disputes between states and investors);
- A relevant provision in the multilateral agreement;
- A rule concerning the arbitration of investment disputes by the ICSID in the national legislation (the Belarusian legislation has no such rule).

Theoretically, even if one of the said grounds is missing, an investor is entitled to file a claim with the ICSID, if, in his opinion, the domestic judicial decisions made by the court of the country, in which he invested, were unfair. Furthermore, because no detailed information concerning the statement made by the Ukrainian national and the Swiss company that he founded is available, it is impossible to say for sure that there was no investment agreement between Belarus and the investors or that the consent to have any disputes resolved through the ICSID was not given otherwise. In any case, a decision will be made in the near future whether the request for arbitration filed with the ICSID is valid and whether the claim to Belarus will be considered employing the dispute-settlement mechanism of the ICSID.

Nevertheless, against the backdrop of the scandal around Belarusian Potash Company, the news that a foreign investor is planning to recover damages against the Republic of Belarus will inevitably cripple the already flawed image of the country and affect the appeal of its market to foreign investors. The new investment dispute involving the entire state rather than a Belarusian enterprise or a local authority is a new landmark in the track record of Belarus as a country with limited investment appeal. Incidentally, Suleiman Kerimov may also challenge the lawfulness of the sale of a portion of his shareholding in Uralkali and take the case to the ICSID referring to it as illegal expropriation.

### **The essence of Mykhailenko's claim**

The former acting director of the foreign Belarus-based enterprise Upeco Industries Gennady Mykhailenko was sentenced to six years in prison subject to property confiscation by the Zheleznodorozhny District Court of the city of Gomel in 2006. The court found Mykhailenko guilty on the ground that when acting as director of Private Unitary Foreign Enterprise (PUIP) Upeco Industries in the period from 2003 to 2004, he took out loans from the Gomel Regional Branch of OAO Belvnesheconombank by false pretences and breach of faith, and misappropriated funds amounting to the difference between the declared and actual value of the equipment that was purchased using the loans, which inflicted losses on the enterprise. The court also found that Mykhailenko produced forged documents that were instrumental in receiving the loan. According to the court, in doing so Mykhailenko misappropriated material valuables and property of the enterprise by false pretences and breach of faith, thus causing large-scale property damage.

Today Mykhailenko claims that the trial was politically motivated and that he never pleaded guilty. A press release posted on the website of the law firm that represents his interests reads that the applicant "suffered severe physical and psychological abuse" during his imprisonment and was subject to inhuman conditions. Mykhailenko also claimed that

"Belarusian officials repeatedly sought to persuade him to relinquish his shareholding in the company".

If the ICSID decides to begin arbitration proceedings, it will need to look into the circumstances of the case and adequacy of the applicant's claims; however, it can already be said that the statements about the political motivation behind the criminal prosecution may not correspond to the facts unless Mykhailenko was involved, directly or indirectly, in the political life of the country or supported, financially or by any other means, political or public figures in the country.

The applicant claims that he is entitled to USD175 million in moral damage and damages to his investment in the Republic of Belarus and collateral damages to other businesses of his. He claims that if successful, he intends to donate "a significant portion of any damages recovered from Belarus to organizations fighting for human rights and the rule of law in the country".

### **Previous investment disputes**

As of today, the most striking examples of disputes between the state and foreign companies operating in Belarus are the cases that resulted in the payment of compensations to the applicants: one case has been registered in the brewing industry (Baltika vs. Krynitsa, USD10.7 million) and the other one is the recovery of outstanding payments (Alfa-Bank vs. Brestenergo, USD18.5 million).

Furthermore, Belarus can "boast" quite a long list of disputes with foreign companies that did not result in any judicial decisions: those pertaining to foreign investments (Lithuanian UBIG vs. Minsk City Administration, USD30 million), the automotive industry (Skoda and Ford), the furniture industry (IKEA), the dairy industry (Danone-Unimilk) and the property market (Itera, Manolium-Processing).

Most of the disputes stem from the lack of legal clarity in Belarus, its complex taxation system, as well as additional conditionality that leads to significant expenses associated with non-core activities.

### **The country's image as a financial asset: the impact of investment disputes**

Amid the situation around the potash row, the investment appeal of the Belarusian economy looks increasingly doubtful. Foreign investors will obviously treat the criminal trial of a foreign business owner as an important indication that existing and potential investments in Belarus are subject to additional risks.

Any commercial dispute can blemish the image of the country, even if the case never reaches the court. In case of a dispute, in which the respondent is the state, rather than a state-run enterprise or a local authority, the impact on the image of the country as an appealing investment destination becomes much more dramatic.

Mykhailenko's request addressed to the ICSID Secretariat is based on the alleged expropriation of his investments resulting from illegal criminal persecution. The odds are high that it will not be recognized as an adequate claim, but will damage the reputation of Belarus even more than the arrest of Uralkali's top manager.