

**THE INTERNATIONAL CENTRE FOR THE SETTLEMENT  
OF INVESTMENT DISPUTES, WASHINGTON, D.C.  
(ICSID CASE NO. ARB/04/6)**

**IN THE ARBITRATION PROCEEDINGS BETWEEN:**

**(1) OKO PANKKI OYJ  
(formerly called: OKO Osuuspankkien Keskuspankki OYJ);**

**(2) VTB BANK (DEUTSCHLAND) AG  
(formerly called: Ost-West Handelsbank AG); and**

**(3) SAMPO BANK PLC**

*First to Third Claimants*

**- and -**

**THE REPUBLIC OF ESTONIA**

*Respondent*

---

**AWARD**

---

*The Arbitration Tribunal:*

**Mr O.L.O. de Witt Wijnen;  
Mr L. Yves Fortier, CC, QC; and  
Mr V.V. Veeder, QC.**

*Secretary to the Arbitral Tribunal:*

**Ms Martina Polasek**

*Date of dispatch to the Parties: November 19, 2007*

## **TABLE OF CONTENTS**

### **PART I: THE PROCEDURAL HISTORY..... 4**

* The Request for Arbitration.....	4
* The Claimants.....	4
* The Respondent.....	4
* The Two BITs.....	4
* ICSID Registration.....	5
* The Tribunal.....	5
* First Session.....	5
* Written Procedure.....	5
* Oral Procedure.....	6
* Costs.....	6
* Post-Hearing.....	6

### **PART II: THE FACTUAL BACKGROUND..... 7**

* 1988.....	7
* 1989.....	7
* 1990.....	8
* 1991.....	8
* 1992.....	9
* 1993.....	10
* The Payment Agreement.....	10
* The [REDACTED] Letter.....	11
* 1994.....	13
* 1995.....	14
* 1996.....	14
* 1997.....	15
* 2001.....	15

### **PART III: THE BANKS' CASE..... 16**

(A) Introduction.....	16
(B) The Alleged Facts.....	16
(C) The Alleged Breaches of the BITs.....	26
(D) The Formal Relief Claimed by the Banks.....	30

### **PART IV: THE RESPONDENT'S CASE..... 32**

(A) Introduction.....	32
(B) The Alleged Facts.....	32
(C) The Alleged Breaches of the BITs.....	43
(D) The Formal Relief Claimed by the Respondent.....	43

### **PART V: THE ISSUES TO BE DECIDED BY THE TRIBUNAL..... 45**

<b>PART VI: ISSUE 1 – JURISDICTION</b> .....	<b>46</b>
(A) Introduction.....	46
(B) The Two BITs .....	46
(i) Was there any Investment at all? .....	48
(ii) Was this Investment made in Estonia? .....	49
(iii) Does the Definition of such an investment apply to investments made before the BITs' entry into force? .....	50
(iv) The Validity of the Banks' Investment .....	50
(C) Can the Estonia-Germany BIT Apply to the Second Claimant's Claims? .....	51
(D) Article 25 (1) of the ICSID Convention .....	53
 <b>PART VII: ISSUE 2 - WAS THERE A BREACH OF THE BITS?</b> .....	 <b>57</b>
(A) Introduction.....	57
(B) Fair and Equitable Treatment: Relevant Legal Principles .....	58
* Autonomous Standard.....	59
* "International Law" .....	64
(C) Fair and Equitable Treatment: Relevant Facts.....	70
(D) The Tribunal's Decision .....	78
 <b>PART VIII: ISSUE 3 - DID THE BANKS FRUSTRATE THE BARGAIN?</b> .....	 <b>81</b>
 <b>PART IX: ISSUE 4 - DAMAGES</b> .....	 <b>84</b>
(A) Introduction.....	84
(B) The Banks' Position .....	84
(C) The Respondent's Position .....	88
(D) The Tribunal's Decision .....	90
* Damages (Principal Amount) .....	95
* Compound Interest.....	95
* The ESVA Proceeds .....	100
* The "Heinaste" Proceeds.....	102
* Expenses .....	102
* Further Compound Interest .....	103
 <b>PART X: LEGAL AND ARBITRATION COSTS</b> .....	 <b>104</b>
 <b>PART XI: THE OPERATIVE PART</b> .....	 <b>107</b>

## ***PART I: THE PROCEDURAL HISTORY***

1. ***The Request for Arbitration:*** On 15 December 2003, the International Centre for Settlement of Investment Disputes received a Request for Arbitration dated 10 December 2003 from OKO Osuuspankkien Keskuspankki Oyj (now called OKO Pankki Oyj), Ost-West Handelsbank AG (now called VTB Bank (Deutschland) AG) and Sampo Bank Plc, as Claimants.
2. ***The Claimants:*** The Claimants were two banks organized under the laws of Finland (OKO Osuuspankkien Keskuspankki Oyj and Sampo Bank Plc) and a third bank organized under the laws of Germany (Ost-West Handelsbank AG). In this Award, these three parties are collectively called “the Banks”.
3. In these arbitration proceedings, the Banks were represented by Mr Patrik Lindfors, Ms Petra Kiurunen and Mr Antti Summa of Hannes Snellman Attorneys at Law Ltd, Helsinki, Finland.
4. ***The Respondent:*** The Respondent is the Republic of Estonia (called in this Award “the Respondent” or “Estonia”).
5. In these arbitration proceedings, the Respondent was represented by Mr D. Brian King, Mr Georgios Petrochilos, Ms Yasmin Mohammad and Ms Laura Halonen of Freshfields Bruckhaus Deringer, Amsterdam and Paris respectively, and by Mr Ilmar-Erik Aavakivi of the Law Office Aivar Pilv, Tallinn, Estonia.
6. ***The Two BITs:*** The Request for Arbitration invoked the provisions of two separate Bilateral Investment Treaties: (i) the Agreement between the Government of the Republic of Finland and the Government of the Republic of Estonia for the Promotion and Protection of Investments (called “the Estonia-Finland BIT” in this Award) which entered into force on 2 December 1992; and (ii) the Agreement between the Federal Republic of Germany and the Republic of Estonia on the Promotion and Mutual Protection of Investments (“the Estonia-Germany BIT”) which entered into force on 12 January 1997.

7. **ICSID Registration:** On 20 February 2004, the Secretary-General of ICSID registered the Banks' Request pursuant to Article 36(3) of the ICSID Convention and, on the same date, notified the Parties of such registration.
8. **Tribunal:** The Request for Arbitration recorded under Section III, the Parties' written agreement regarding the constitution of the Tribunal, which was subsequently confirmed by the Respondent on 24 February 2004. The Parties agreed that the Tribunal was to consist of three arbitrators: Mr O.L.O. de Witt Wijnen, as the President of the Tribunal appointed by both Parties; Mr V.V. Veeder, Q.C., Co-Arbitrator appointed by the Banks; and Mr L. Yves Fortier, C.C., Q.C., Co-Arbitrator appointed by the Respondent. The Parties were notified on 8 March 2004 by ICSID that the Tribunal was constituted and that the proceedings had begun on that date in accordance with Rule 6(1) of the ICSID Rules of Procedure for Arbitration Proceedings (here called "the ICSID Arbitration Rules"). Pursuant to Regulation 25 of the ICSID Administrative and Financial Regulations, the Parties were also informed that Ms Martina Polasek, Counsel of ICSID, would serve as Secretary of the Tribunal.
9. **First Session:** With the agreement of the Parties, the first session of the Tribunal was held at The Hague, the Netherlands, on 10 May 2004. On that occasion, the Parties agreed on a number of procedural matters reflected in minutes signed by the President and the Secretary of the Tribunal. Among other items, it was agreed that the procedural language would be English and that the place of proceedings would be The Hague, but that the Tribunal might organize hearings and sessions at a different venue, after consultation with the Parties. It was also agreed that in the conduct of the proceedings, the Parties and the Tribunal should be guided by the Rules on the Taking of Evidence in International Commercial Arbitration adopted by the International Bar Association on 1 June 1999 ("the IBA Rules"), in addition to the application of the ICSID Convention and the ICSID Arbitration Rules.
10. **Written Procedure:** In accordance with the timetable agreed at the first session of the Tribunal, on 15 July 2004 the Banks filed their Memorial. Following the Respondent's indication that it intended to file jurisdictional objections, the

Tribunal allowed the Respondent to join such objections to its Counter-Memorial on the merits to be filed by 17 November 2004. The Counter-Memorial, including jurisdictional objections and supporting documents, was filed on 19 November 2004. The Tribunal held a telephone conference with the Parties on 21 December 2004 to discuss the timetable and further procedure. It was agreed that the Respondent's jurisdictional objections would be joined to the merits of the case; that accordingly the Banks would submit their Reply on the merits and jurisdiction by 31 January 2005; and that the Respondent would submit a Rejoinder by 15 April 2005. The Banks filed their Reply on 31 January 2005; and the Respondent filed its Rejoinder on 29 April 2005, after an extension of time granted by the Tribunal.

11. **Oral Procedure:** On 10 June 2005, following submissions made by the Parties, the Tribunal issued directions regarding the oral procedure. With the Parties' agreement, the main hearing on jurisdiction and the merits was held in Paris from 16 to 21 October 2005 ("the Hearing"). This Hearing included the oral examination of witnesses and experts.
12. **Costs:** In accordance with the Tribunal's directions and the Parties' agreement, the Parties filed written submissions on legal and arbitration costs simultaneously on 8 March 2006 and reply submissions on costs (also simultaneously) on 17 March 2006.
13. **Post-Hearing:** The Parties also exchanged correspondence by letters of 16 and 20 February 2006 and 1, 10 and 17 March 2006 on, notably, the quantum of damages claimed by the Banks.
14. By letter of 28 September 2006 the Tribunal was informed of a change of name of the First and Second Claimants.
15. On 9 October 2007, the Tribunal declared the proceedings closed pursuant to ICSID Arbitration Rule 38.

## ***PART II: THE FACTUAL BACKGROUND***

16. The relevant factual events straddle a turbulent period of European history, from 1988 (when Estonian territory was still occupied by the USSR) to August 1991 and onwards (when the Respondent re-emerged as an independent sovereign state). The following chronology is established on the evidence adduced by the Parties in these arbitration proceedings.
17. **1988:** On 6 April 1988, a legal entity called Estrôbprom (the Estonian Industrial Shipping Company, established in the Estonian Soviet Socialist Republic of the USSR), and a Finnish company called Valio Oy (here called “Valio”) established a joint venture company by the name of ESVA. The purpose of ESVA was to build a fish-processing factory in Tallinn, in the Estonian SSR, then part of the USSR.
18. **1989:** On 4 January 1989, the Banks granted to ESVA an interest-bearing loan in accordance with the terms of a loan agreement (here called “the Loan Agreement”) up to the equivalent of 93,000,000.00 Finnish Markka, to be made available in respectively U.S. Dollars (1 x 31,000,000 FIM) and German Marks (2 x 31,000,000 FIM).
19. The Loan was granted by the Banks in equal portions, *i.e.* the equivalent of FIM 31 million was made available in USD by the First Claimant, OKO Pankki Oyj, and in DEM by the Second and Third Claimants, VTB Bank (Deutschland) AG and Sampo Bank PLC respectively. Repayment under the Loan Agreement was to start on 4 July 1991 and was to continue for ten years, until 2000. The Loan Agreement was governed by Finnish Law.
20. As a condition precedent to the Loan, the two parties to the ESVA joint venture agreement, Valio and Estrôbprom, issued Guarantees as security for the Loan. Valio guaranteed 48 % and Estrôbprom 52 % of the Loan. These two Guarantees were unconditional, irrevocable and independent obligations to pay any amounts

due under the Loan on first written demand by the Banks. The Guarantees were governed by Finnish law.

21. In November 1989, the employees of Estrôbprom and the USSR Ministry of Fishing Industry (to which the former was administratively subordinate) concluded a rental agreement according to which Estrôbprom and its assets were rented to the collective of Estrôbprom's employees for five years as of 1 January 1990.
22. **1990:** On 15 October 1990, the Tallinn City Council registered the rental agreement and its Articles of Association as “Eesti Kalatööstus” (the Estonian Fish Processing Association, here called: “Eesti Kalatööstus”) in the register of enterprises, agencies and organizations of the Estonian SSR. The registration number given to the company was 01007501.
23. **1991:** On 20 August 1991, the Respondent declared its independence from the USSR.
24. On 29 August 1991, the Supreme Council of the Respondent declared the property of any companies, associations or organisations in the territory of Estonia operating under the control or subordination of any Soviet administration as property of the Respondent. On 12 September 1991 the Government of the Respondent passed Decree No. 182 on the implementation of the Supreme Council’s decision. An attachment to the decree listed the companies which (together with their assets) were declared to be the property of the Respondent. Amongst them was Eesti Kalatööstus.
25. Following the dissolution of the USSR and the dismemberment of its state planned economy, ESVA’s operations faced economic difficulties. In particular, Eesti Kalatööstus was no longer able to provide the raw material, *i.e.* the fish, needed for ESVA's factory. ESVA asked the Banks for postponement of the payments due to them under the Loan Agreement.
26. On 18 November 1991, the Board of Eesti Kalatööstus decided to change the latter’s name to Eesti Kalatööstuse Rendikoondis “Ookean” (the Estonian



- Industrial Fishing Company “Ookean”). The new name was registered in the companies register by the City Government of Tallinn on 9 April 1992 with the existing registration number 01007501. This entity was referred to in practice as “RE Ookean”, “RE” standing for the general Estonian term “state enterprise” (Riiklik Ettevöte); and in this Award it is also called “RE Ookean”.
27. **1992:** On 30 September 1992, the Director-General of RE Ookean (Mr [REDACTED]) and its Director of Finance (Mr [REDACTED]) sent a letter to the Banks confirming that the state-owned company RE “Ookean”, registered in the companies register of the Respondent on 9 April 1992 with the registration number 01007501, was the legal successor of the rental company “Eesti Kalatööstus”<sup>1</sup>.
28. On 21 September 1992, the Estonian Ministry of Industry ordered that a state-owned joint-stock company of the first class (RAS) be established on the basis of the state-owned company RE Ookean. In July 1993, the state-owned limited liability company Riiklik Aktsiaselts, or “RAS Ookean” was created, when its Articles of Association dated May 1993 were accepted. On 1 July 1993, the City Government of Tallinn registered this company in the companies register. The registration number remained, as before, 01007501<sup>2</sup>.
29. The economic difficulties confronting ESVA continued. Eventually, ESVA was unable to pay the first instalment of the Loan, which was due in early July 1992 (*i.e.* 30 months from 4 January 1989, pursuant to Article 9(A) of the Loan Agreement).
30. In view of these continuing difficulties, negotiations commenced between the Banks and ESVA to restructure the Loan. However, these attempts failed; and ESVA continued to default on its obligations under the Loan Agreement.

---

<sup>1</sup> Exhibit C13.

<sup>2</sup> Exhibit C23.

31. On 6 October 1992, the Banks sent a written demand for payment to RE Ookean. The demand letter was also sent directly to the Ministry of Economy and the Ministry of Industry of the Respondent<sup>3</sup>.
32. On 16 December 1992, by Notice of Termination, the Banks declared the Loan immediately due and payable by RE Ookean under the Loan Agreement and also presented their claims against the two Guarantors<sup>4</sup>. Valio paid its share under its Guarantee, but Ookean (*i.e.* both RE Ookean and RAS Ookean) did not honour the Second Guarantee. (From this point onward in this Award, where it remains unclear which company was involved, reference will be made indifferently to “Ookean”).
33. On 17 December 1992, Valio filed a bankruptcy petition against ESVA in the Tallinn City Court. The Banks also initiated bankruptcy proceedings against Ookean on 25 February 1993, contending that it bore a responsibility for ESVA's debt under the Guarantee issued by Estrôbprom (which remained unpaid).
34. **1993:** ESVA was declared bankrupt on 18 March 1993 by the Tallinn City Court. The Estonian Ministry of Economy appealed against this decision.
35. During the summer of 1993, the Banks continued to meet with representatives of the Estonian Ministry of Economy and Ookean to discuss the reorganisation of ESVA and the repayment of ESVA's Loan.
36. The Banks filed an action against Ookean in the City Court of Helsinki in June 1993, in order to retain their rights under the Guarantee. This action was postponed several times due to the Banks' further negotiations with the Estonian Government and Ookean.
37. ***The Payment Agreement:*** On 17 September 1993, RAS Ookean and the Banks signed an agreement on the rescheduling and repayment of the Banks' debt due under the Loan Agreement, here referred to the “Payment Agreement”<sup>5</sup>. The Payment Agreement identified the outstanding total amount of the Loan at DEM

---

<sup>3</sup> Exhibits C14; C15.

<sup>4</sup> Exhibit C16.

<sup>5</sup> Exhibit C26.

15,441,892.98 and USD 4,147,801.49. The Payment Agreement was governed by the law of Sweden.

38. In the Payment Agreement, RAS Ookean undertook (*inter alia*):
- (1) To repay to the Banks the outstanding Loan, together with interest pursuant to the Loan, until the date of final payment. In consideration of this undertaking, the Banks' legal proceedings against Ookean in Tallinn and Helsinki and against ESVA in the Supreme Court of Estonia would be terminated;
  - (2) To sell six of its vessels, in order to raise funds for the settlement of the Loan<sup>6</sup>;
  - (3) To provide to the Banks, not later than 30 September 1993, as security for the Loan and for fulfilment of Ookean's obligations under the Payment Agreement first priority mortgages, in form and substance satisfactory to the Banks, on the vessels;
  - (4) To acquire all official, governmental or company consents or approvals required for the signing of the Payment Agreement and sale of the vessels; and
  - (5) To sell the vessels and repay the Loan fully as soon as possible and without any undue delay (but in any case by 31 December 1997), in accordance with a time schedule set out in the Payment Agreement.

There were further provisions for default, an escrow arrangement, insurance and transfer of the Banks' rights and obligations in ESVA's bankruptcy estate upon receiving payments in accordance with the Payment Agreement, together with a provision that a representative of Ookean would attend the creditors' meeting of the ESVA bankruptcy estate.

39. **The [REDACTED] Letter:** RAS Ookean also undertook to deliver to the Banks, on signing of the Payment Agreement, a letter by the Estonian Ministry of Economy

---

<sup>6</sup> These vessels were named in the Payment Agreement (as later amended).

in the following terms<sup>7</sup> (for ease of later reference, square paragraph numbers have here been added):

*“[1] Ookean Ltd is a state-owned limited liability company in good standing incorporated under the laws of the Republic of Estonia. It has full power and authority to enter the above agreement and to perform and to implement the same. All corporate acts and governmental approvals for signing and implementing the Agreement will be presented to the government of the Republic of Estonia.*

*[2] Ookean Ltd shall have all necessary permissions and approvals from the Estonian authorities, in form and substance satisfactory to the banks, to sell and pledge the vessels, listed in schedule no. 1 of the above agreement, and use all funds from the sale of these vessels for the purpose of repaying the ESVA Loan in accordance with the above agreement.*

*[3] The Board of Ookean shall through their capacity and the authority invested in them by the Ministry, exercise their rights and powers in such a manner as to ensure that Ookean Ltd complies with the obligations stipulated in this agreement.”*

40. In accordance with the Payment Agreement, a letter in these terms was delivered to the Banks also dated 17 September 1993, signed by Mr [REDACTED] then the Estonian Minister of Economy (here called “the [REDACTED] Letter”). It will be necessary to return to the terms of this letter below; but it is sufficient to note here that its existence, as a collateral side-letter, demonstrates unequivocally that the Respondent was not (and was not intended to be or to become) a principal obligor under the Payment Agreement, Loan Agreement or Estrôbprom Guarantee.
41. Also in accordance with the Payment Agreement, RAS Ookean presented the Payment Agreement to the Tallinn City Court and requested the termination of the bankruptcy proceedings against it on the basis of the settlement reached with the Banks. The Court granted that request with the Banks’ consent; and it confirmed the termination of the bankruptcy proceedings against Ookean on 25 November 1993 on the basis of the Payment Agreement. The legal proceedings in the Helsinki Court were also eventually withdrawn.

---

<sup>7</sup> Schedule 2 to the Payment Agreement, Exhibit C26.

42. Meanwhile, in December 1993, the Banks and Valio had established a new company called Paljassaare Kalatööstus A/S (here called “Paljassaare”), which was to buy the assets and operations of ESVA from the bankrupt estate. This acquisition was later implemented by the Banks.
43. **1994:** On 4 March 1994, a mortgage contract (in Estonian “Pandileping”) was concluded by RAS Ookean relating to the six vessels which were to be sold pursuant to the Payment Agreement. According to that contract (here called “the Mortgage Contract”), RAS Ookean undertook to mortgage the vessels and present the relevant application to the Estonian Ship Registry<sup>8</sup>.
44. On 4 April 1994, the Respondent issued a decree to the effect that the vessels pledged to the Banks were to be sold in order to enable RAS Ookean to repay its debts to the Banks. That decree was signed by the Respondent’s Prime Minister and published in the Estonian Statute Book.
45. The Estonian Ministry of Economy undertook to give its permission to sell the vessels by 15 July 1994.
46. The six mortgages on the vessels remained unregistered, notwithstanding the Banks’ best efforts. On 13 May 1994 the Banks sent a letter to the Estonian Ministry of Economy asking the Ministry to see that RAS Ookean adhered to the Payment Agreement and the Mortgage Contract.
47. The mortgages on the six vessels were eventually registered in the Ship Register of the Estonian National Maritime Board on 15 July 1994.
48. The Payment Agreement stipulated that the first vessel was to be sold and a minimum amount of USD 2,000,000.00 of the sale proceeds was to be repaid to the Banks by 31 December 1994. This undertaking was not satisfied by RAS Ookean. One of the vessels had meanwhile been arrested in Namibia. The Banks used their right pursuant to the Payment Agreement to seek buyers for the mortgaged vessels.

---

<sup>8</sup> The Tribunal adopts the English translation in Exhibit C38.

49. **1995:** In October 1995, three other vessels were arrested in South Africa.
50. On 10 February 1995, one of the vessels, the “Heinaste”, was sold for USD 2,177,856.68. The Banks received from these proceeds the sum of USD 662,143.00. It was agreed that the Banks’ debt due from RAS Ookean would be reduced by USD 2.8 million.
51. On 20 October 1995, RAS Ookean filed a petition in the Tallinn City Court, requesting the Court to declare the Payment Agreement and the Mortgage Contract invalid.
52. On 30 October 1995, RAS Ookean was declared bankrupt at the request of the Port of Tallinn. The trustees in bankruptcy did not accept the Banks as creditors. Legal action taken by the Banks against this refusal did not succeed.
53. In December 1995, the vessel “Georg Kask” was sold for approximately USD 1 million; and the vessel was removed from the Ship Register of Estonia, free of any encumbrances.
54. On the application of the trustees in RAS Ookean's bankruptcy, the Tallinn City Court granted, on 4 December 1995, a discharge of the mortgages registered in favour of the Banks. The Estonian Ship Register deleted the mortgages on the basis of this decision.
55. **1996:** The Banks appealed from this decision of the Tallinn City Court; and on 21 February 1996 the District Court revoked the decision of the City Court with regard to the deletion of the mortgages from the Ship Register. The Estonian Supreme Court upheld the District Court’s decision on 22 May 1996, in favour of the Banks.
56. After legal proceedings in South Africa and negotiations held in London between the Banks and the RAS Ookean bankruptcy estate, the vessels named “Moonsund” and “Georg Lurich” were sold by a private sale confirmed by the Court. In response to the bankruptcy estate’s demand, the proceeds from these transactions were frozen by a decision of the South African Court. Two other

- vessels, the “Stralsund” and “Eestirand II” were sold on 10 May 1996 and removed from the Estonian Ship Register on 14 May 1996.
57. On 28 August 1996 the Tallinn City Court declared the Payment Agreement and the Mortgage Contract invalid. The Banks were ordered to return to the bankruptcy estate the amount received from the sale of the “Heinaste” of USD 2.8 million and, in addition, to pay stamp duty in the sum of EEK 14.5 million.
  58. **1997:** On 5 December 1997, the District Court annulled the decision of the Tallinn City Court and declared valid and binding the Payment Agreement and Mortgage Contract between the Banks and RAS Ookean.
  59. **2001:** After a number of appeals and other numerous legal skirmishes, the Supreme Court of Estonia, on 16 November 2001, declared the Payment Agreement and Mortgage Contract invalid.
  60. The balance of the Loan was not repaid to the Banks and remains unpaid.

### ***PART III: THE BANKS' CASE***

#### ***(A) Introduction***

61. The Banks contend that the dispute between the Parties is a legal dispute arising directly out of an investment made by the Banks as defined in the ICSID Convention and the two BITs: the Estonia-Finland BIT and the Estonia-Germany BIT.
62. The Banks contend that all relevant requirements for their claims under these two BITs are fulfilled (as to both jurisdiction and merits); they had an investment in Estonia, this investment was frustrated by the Respondent in a manner violating the BITs and international law; and the Respondent is therefore responsible to the Banks for the damages caused by its acts and omissions.

#### ***(B) The Alleged Facts***

63. According to the Banks' case, the Banks' investment was the aggregate of (i) the Loan initially extended to ESVA in 1989, (ii) the Guarantee issued by Estrôbprom (of which RAS Ookean was the legal successor) which secured the payments under the Loan Agreement, (iii) the Payment Agreement and (iv) the Mortgage Contract, the last two rescheduling and further securing the payments due to the Banks.
64. The Banks based their decisions to grant the Loan and to accept the Guarantee, to a large extent, on information which Estrôbprom provided as to its assets. According to the information received by the Banks, these assets were considerable and sufficient to ensure that Estrôbprom was capable of fulfilling its obligations under the Guarantee. In a letter dated 29 November 1988, the Director-General of Estrôbprom confirmed that the assets of Estrôbprom included, amongst other properties, an ocean fleet consisting of 57 vessels, a



fishing factory in Pärnu, a fishing harbour in Tallinn, a shipyard, a fishing equipment factory and a cold storage.

65. After the Respondent's independence in August 1991, ESVA's operations faced difficulties because Eesti Kalatööstus was not able to provide the fish needed for its factory. ESVA asked the Banks for a postponement of its payment due under the Loan Agreement. The Banks then approached the Respondent's Department of State Property, expressing their concern over the situation at ESVA and Eesti Kalatööstus. The Banks indicated that, despite the reorganisation of Eesti Kalatööstus, the Respondent should ensure that the company was allowed to keep sufficient assets to support the Guarantee given to the Banks.
66. During 1991 and 1992, the Banks had several meetings with Estonian governmental authorities and RE Ookean regarding the status of both ESVA and RE Ookean. ESVA's difficulties nonetheless continued; and it failed to make the payments due under the Loan Agreement. At these meetings, representatives of the Respondent assured the Banks that they would not suffer any losses if they refrained from taking legal actions for the recovery of the payments due to them.
67. Following further negotiations between the Banks and the Respondent, the Banks sent to Ookean, on 6 October 1992, a written demand for payment. The demand letter was also sent to the Ministry of Economy and the Ministry of Industry of the Respondent.
68. When Valio filed the bankruptcy petition against ESVA in December 1992, the proceedings were postponed at the request of Ookean until an opinion from the Ministry of Economy was received. The Banks then once again approached the Respondent, asking the Ministry of Economy to support this request so that a reorganisation of ESVA's operations would be possible.
69. ESVA was declared bankrupt on 18 March 1993 by the Tallinn City Court. The Ministry of Economy appealed against the Court's decision on 29 March 1993 and requested that its enforcement be postponed. The grounds given for the appeal were first that ESVA had enough financial resources to avoid bankruptcy and, secondly, that Ookean had during the bankruptcy proceedings before the

Court offered to sell six “Moonsund”-type vessels to cover the debts of ESVA. The Ministry of Economy stated that it had approved this proposal from Ookean.

70. In further meetings during the summer of 1993, intended to find a solution, representatives of the Respondent again promised that the Respondent would honour the Guarantee and that the obligations under that Guarantee would be paid in full. Trusting the Respondent's promises, the Banks agreed to postpone the bankruptcy proceedings of Ookean. Several repayment options were discussed, but the main solution offered by Ookean and the Respondent was the sale of Ookean's vessels. These discussions were conducted from the premise that an agreement on repayment of the loan would be made between the Respondent, Ookean and the Banks.
71. After assurances from the Respondent that it would be sufficient if the agreement was concluded only between the Banks and Ookean, these negotiations resulted in RAS Ookean and the Banks signing the Payment Agreement on 17 September 1993, at the premises of the Estonian Ministry of Economy in Tallinn.
72. According to the Payment Agreement, RAS Ookean committed itself to paying to the Banks the remaining balance of the Loan (with interest until the date of final payment). Under the agreed payment schedule, RAS Ookean's payments should have been made to the Banks by 31 December 1997.
73. In the Payment Agreement, RAS Ookean also represented and warranted to the Banks that it was: “[...] *validly existing, duly incorporated and registered limited liability company, whose equity is 100% beneficially owned by the Republic of Estonia [...]*”; and RAS Ookean further warranted that: *"it has full authority and power to enter into and implement the Agreement and that all corporate and governmental actions, approvals and authorisations for the signing and implementation of the agreement had been made and exist."*<sup>9</sup>

---

<sup>9</sup> Exhibit C26.

74. According to Article II.4 of the Payment Agreement, the Banks were to be granted first priority mortgages on the vessels, as a security for the Loan and the fulfilment of RAS Ookean's obligations.
75. In connection with the Payment Agreement, on the same date, the Ministry of Economy issued a letter signed by Minister [REDACTED] for the Respondent confirming that (i) Ookean had the capacity to conclude and implement the Payment Agreement; (ii) Ookean would have all the necessary permissions to sell and pledge the vessels; and (iii) that the Board of Ookean, through the capacity and authority invested in it by the Ministry, would ensure that the Payment Agreement was complied with. It is the Banks' case that the [REDACTED] Letter constituted a binding commitment made by the Respondent to the Banks.
76. However, the mortgaging and sale of the vessels did not proceed as agreed under the Payment Agreement. The Banks first approached RAS Ookean (with a copy to the Ministry of Economy) and called for compliance with the Payment Agreement.
77. The Banks also met representatives of RAS Ookean to discuss the situation with regard to the sale and mortgage of the vessels. RAS Ookean's General Director, (Mr [REDACTED]), informed the Banks that RAS Ookean was still waiting for the Estonian Government's permission.
78. During these meetings the Banks learned that the assets of Ookean were constantly being transferred out of that company by the Respondent. The Banks sent a letter addressed to the Ministry of Economy and the Ministry of Transportation and Communication stating their concern over the draining of Ookean's assets and urging that the Respondent attend to the interests of the Banks, in accordance with the [REDACTED] Letter.
79. The following substantial assets were transferred out of the company after 1993, (if not more):
- (1) The Pärnu Fish Processing Factory was transferred out of RAS Ookean and later privatised;

- (2) The Tallinn Sailors Hospital and Outpatient Department was transferred to the City of Tallinn; and
  - (3) The Kopli Port was transferred to the Port of Tallinn, a state-owned entity;
  - (4) The cold storage was also transferred to the Port of Tallinn; and
  - (5) The fleet of fishing vessels mostly vanished.
80. During the summer of 1994 the Banks attended further meetings with the Estonian Ministry of Economy. In these meetings the Respondent again repeated its promise that the interests of the Banks would not be hurt and that the obligations of RAS Ookean towards the Banks would be fulfilled.
81. On 28 and 29 June 1994 the Banks and the Estonian Ministry of Economy met to discuss and agree on the timetable and measures to be taken for the repayment of the Loan. It was agreed that the Banks would arrange an assignment contract between RAS Ookean and a brokerage company for the purpose of selling the vessels. The Estonian Ministry of Economy undertook to give its permission to sell the vessels by 15 July 1994. It was also agreed that Mr [REDACTED] from the Ministry of Economy would ensure that the mortgages were registered in accordance with the Mortgage Contract.
82. During discussions on the future and reorganisation of ESVA, which eventually led to the establishment of Paljassaare, the Estonian Ministry of Economy continued to assert that matters would be taken care of in a manner satisfactory to the Banks.
83. During discussions over the sale of the vessels, a representative of the Estonian Ministry of Economy, (Mr [REDACTED]), stated that the Respondent would be prepared to pledge other vessels of RAS Ookean as additional security to the Banks in case the value of the Mortgage Contract decreased due to the legal seizure of the vessels in Namibia.
84. In April 1995, RAS Ookean presented a “compromise offer”, whereby the Banks would be required to cancel the mortgages on the remaining five vessels. In

- return RAS Ookean would repay USD 6 million to the Banks by the end of 1995, either by selling three vessels or by other means. RAS Ookean would also have transferred to the Banks its claim of recourse in the bankruptcy estate of ESVA. According to RAS Ookean (as contended by the Banks), the reason for the compromise offer was that the economic situation had changed since 1993 and that RAS Ookean was now in a position to repay the debt due to the Banks with other assets.
85. On 11 September 1995, the Banks' legal representative (Mr ██████████) met Mr ██████████ of the Estonian Ministry of Economy. Mr ██████████ informed Mr ██████████ that the Ministry was aware of the compromise offer and that Mr ██████████ had all the necessary powers to act on behalf of RAS Ookean and the Ministry of Economy. Mr ██████████ further stated that RAS Ookean had other assets besides the pledged vessels and that everything could be negotiated amicably with the Banks. The Banks agreed to further negotiations.
86. To the Banks' surprise, RAS Ookean was then declared bankrupt on 30 October 1995 within a few weeks after the Banks' meeting with Mr ██████████. The bankruptcy petition was filed by the Port of Tallinn; and RAS Ookean did not oppose that petition. Mr ██████████ was appointed assistant to the trustees of the bankruptcy estate (Mr ██████████).
87. After RAS Ookean's bankruptcy, negotiations concerning the sale of the vessels continued between the Banks and different Estonian authorities. However, there came a point when the Banks were not recognised as creditors in this bankruptcy. The Banks challenged this decision without success.
88. On 29 January 1996, the Banks met the bankruptcy trustees to discuss the situation. At this meeting, the trustees stated that they would be willing to acknowledge the validity of the Payment Agreement and the Mortgage Contract if the Banks were to withdraw their appeal regarding the deletion of the mortgage registrations. The trustees also stated that should the Banks postpone the compulsory auction of the "Georg Lurich" and the "Moonsund", the trustees

- would be willing to allow the Banks the status of creditors in the bankruptcy estate.
89. The Banks also learned that ten days before the bankruptcy decision relating to RAS Ookean, the Management Board (which consisted mainly of representatives of the Respondent) had filed a petition to the Tallinn City Court asking the Court to declare the Payment Agreement and the Mortgage Contract invalid. Furthermore, on the application of the trustees, the Tallinn City Court granted, on 4 December 1995, a discharge of the mortgages registered in favour of the Banks. The Estonian Ship Registry then deleted the mortgages pursuant to the Court's decision. The Banks were not heard in these procedures.
  90. On 21 February 1996, upon the Banks' appeal, the District Court revoked the decision of the City Court with regard to the deletion of the mortgages from the Ship Register. The Estonian Supreme Court upheld the District Court's decision on 22 May 1996.
  91. On 28 August 1996, the Tallinn City Court granted RAS Ookean's claim and declared the Payment Agreement and the Mortgage Contract invalid. The City Court further ordered the Banks to return the sale proceeds of the "Heinaste" in the sum of USD 2.8 million. In addition, the Banks were ordered to pay stamp duty in the amount of EEK 14.5 million (approximately EUR 1 million at that time).
  92. The Banks considered the imposition of stamp duty to be arbitrary and unlawful and, therefore, paid stamp duty in the amount of EEK 200 only and appealed against the decision of the City Court. The Banks asserted that the dispute was "non-valued", which meant that, in accordance with the Estonian Act on Civil Proceedings and the Act on Stamp Duty, the duty to be paid was EEK 100 for a claim regarding the conclusion, amending or ending of a contract. As the claim concerned two contracts, the duty to be paid was, according to the Banks, EEK 200 only.
  93. The Tallinn City Court rejected the Banks' appeal with regard to unpaid stamp duty. The Banks appealed against the City Court's decision; but the District

- Court upheld the City Court's decision. The Estonian Supreme Court ruled that the dispute was in fact "non-valued" but ordered the Banks to pay stamp duty in the amount of 3% of the sale price of the "Heinaste" and returned the matter to the District Court. The District Court then ruled that the Banks were to pay a sum of EEK 994,703.00 (approximately EUR 63,000) as stamp duty. The Banks paid this amount and appealed to the District Court.
94. On 5 December 1997, the District Court annulled the decision of the Tallinn City Court and declared the agreements between the Banks and RAS Ookean to be valid and binding.
  95. RAS Ookean appealed against this decision; and as a result, the Estonian Supreme Court returned the case to the District Court on 22 April 1998, stating that its decision was insufficiently reasoned.
  96. The District Court issued a new decision on 12 June 1998, again declaring the agreements to be valid and binding. RAS Ookean appealed for the second time.
  97. While these court proceedings were taking place, the Banks continued to negotiate for a settlement with the bankruptcy estate. During the autumn of 1998, the bankruptcy committee informed the Banks that it was in principle in favour of a settlement, but that the opinion of the Estonian Government had to be obtained before any decision could be made. In October 1998, the bankruptcy committee accepted a draft settlement agreement drawn up by the trustees of the estate. Settlement was, however, never agreed with the Banks. For reasons unknown to the Banks, the bankruptcy estate became reluctant to continue the negotiations.
  98. On 9 November 1999, the District Court gave its third decision on the validity of the Payment Agreement and Mortgage Contract, again in the Banks' favour. This decision (like the two previous ones) was overturned and returned by the Supreme Court to the District Court for retrial.
  99. On this fourth occasion, the District Court changed its ruling; and, on 6 April 2001, declared the Payment Agreement and Mortgage Contract invalid. The

Banks appealed; and this time the Estonian Supreme Court agreed with the District Court.

100. According to the Supreme Court's decision of 16 November 2001, the evidence on which the Banks based their arguments regarding legal succession from Estrôbprom to Ookean was insufficient to conclude that the rights and obligations of Estrôbprom/Eesti Kalatöötuse were transferred to Ookean. The Supreme Court also stated, with reference to the District Court's decision, that the agreements between the Banks and RAS Ookean were invalid due to non-compliance with the law, which was the basis for the activities of a state-owned public limited company. RAS Ookean was, according to the Court, not permitted to enter into obligations for a third party's debt; and thus the agreements concluded with the Banks exceeded RAS Ookean's legal capacity. Regardless of the [REDACTED] Letter and the Government Order 204-k, the Supreme Court also concluded that the Government of the Respondent had not granted to RAS Ookean the requisite permission to conclude the disputed transactions. As regards the sale of the "Heinaste", the Supreme Court stated that the Government of the Respondent had indeed given its permission for the sale of RAS Ookean's vessels and for the use of the sale proceeds to pay the debts of RAS Ookean. However, according to the Supreme Court, it had not been ascertained that RAS Ookean was indebted to the Banks nor did the Government of the Respondent give its permission to use the proceeds of the sale to pay the debts to the Banks.
101. The Banks were accordingly ordered to return to the bankruptcy estate the monies received from the sale of the "Heinaste" in the amount of USD 2.8 million (thereby including the amount which had in fact not been paid to the Banks); to compensate the bankruptcy estate's expenses in the amount of EEK 90,000; and to pay state fees in the sum of EEK 386,603.35. The Banks complied with the Supreme Court's decision (with a statement indicating no waiver of its rights) and made the relevant payments on 20 February 2002.
102. As a result of the events described above, the Banks lost almost half of their original Loan plus the expected proceeds of that Loan, *i.e.* interest according to the Loan Agreement. Moreover, the Banks had to pay an extra USD 622,143.32



- to the bankruptcy estate of RAS Ookean without any valid cause. In addition, the Banks suffered significant losses in the form of expenses and fees due to the several court proceedings described above.
103. On several occasions in the negotiations during the bankruptcy proceedings of ESVA, the representatives of the Respondent made promises to the Banks stating that the Respondent would honour the Guarantee and that obligations under it would be paid in full. Eventually, this gave rise to the clear commitment in the [REDACTED] Letter. The message given by the Respondent to the Banks was explicit: the debt under the Guarantee would be paid to the Banks. However, these promises were not complied with by the Respondent.
104. In fact, from the moment that ESVA was unable to repay the Loan, the Banks have been in continuous contact and have continuously and intensively negotiated not only with the representatives of ESVA and Ookean (and their bankruptcy trustees), but also with the Respondent in order to find an amicable solution for the repayment of the Loan. Repeatedly, those representatives, including the representatives of the Respondent, have assured the Banks that the Loan to ESVA would be repaid. On account of those assurances, the Banks were willing, at several points in time, to postpone and withdraw legal action. These assurances culminated in the conclusion of the Payment Agreement and the delivery of the [REDACTED] Letter, as described above.
105. Thereafter, however, RAS Ookean and the Respondent continued not to comply with their obligations. Notably, the payment schedule under the Payment Agreement, and the mortgaging and sale of the vessels was not properly respected. When reasonable offers were received for the six vessels, RAS Ookean and the Respondent refused to accept them. They also refused to liquidate other resources of RAS Ookean in order to repay the debt due to the Banks.
106. At the same time, RAS Ookean's assets were depleted. Originally, at the time of its incorporation, RAS Ookean had assets with a book value of almost EEK 500 million, *i.e.* approximately EUR 32 million. Moreover, attached to its Articles of

Association was a list of RAS Ookean's assets. These assets included fifty vessels, a shipyard, a refrigeration plant, a hotel, a car depot, navigation unit *etc.* The stated book value of these assets was EEK 462,471,000.

107. When RAS Ookean was eventually declared bankrupt, the Respondent dominated the bankruptcy estate; and the Banks were excluded from the list of creditors.
108. The Banks submit that all the actions of the Respondent, either directly or through Ookean, led the Banks to postpone the collection of their debt for many years, drove the Banks to several court proceedings in Estonia and finally caused the Banks to lose a major part of their investment by, in reality, nullifying the Guarantee. At the same time the Respondent took the benefit of Ookean's substantial assets as Guarantor.
109. The changes made to Ookean's assets over the course of time are, however, not relevant to their dispute. What is relevant is that Ookean and its assets were at all times fully owned and controlled by the Respondent and that the Respondent exercised its control over Ookean actively, *e.g.* by negotiating with the Banks as to the obligations of Ookean under its Guarantee, by transferring Ookean's assets to other state-owned companies while at the same time refraining from repayment to the Banks and by causing Ookean to enter into agreements that were later treated as invalid by the Estonian Courts.

***(C) The Alleged Breaches of the BITs***

110. According to the Banks' case, all of the individual acts on the Respondent's side, both with regard to its own conduct and by its control of Ookean, in part and in aggregate whole, constitute breaches of several provisions of each of the two applicable BITs, notably those providing full security and protection and ensuring fair and equitable treatment to the investment, those forbidding nationalisation or expropriation without due compensation and those requiring that commitments made regarding the investment are honoured. In the same manner as the underlying facts constituting the Respondent's liability are intertwined and breach

the BITs as a whole, the relevant provisions of the BITs apply to most of the actions and omissions of the Respondent during the disposal of Ookean's assets. This is notably true as regards Articles 3, 4 and 5 of the Estonia-Finland BIT and Articles 2, 4 and 8 of the Estonia-Germany BIT.

111. With regard to the Tribunal's jurisdiction, the Banks contend first of all that the assessment of whether the Banks had an “investment” must be based on their overall operations in Estonia. The Banks refer in this context to the *CSOB* case in which it was decided that: “...*a dispute that is brought before the Centre must be deemed to arise directly out of an investment even when it is based on a transaction which, standing alone, would not qualify as an investment under the Convention, provided that the particular transaction forms an integral part of an overall operation that qualifies as an investment.*”

112. In that light, there can be no doubt that the Banks did have an investment (in Estonian territory):

- (1) In 1989 a modern factory was built using the Banks' monies;
- (2) From 1989 onwards, the Banks participated in the project as financiers;
- (3) From 1993 onwards, the Banks were majority owners of a major factory (first through the bankruptcy estate, then Paljassare);
- (4) The Payment Agreement, the Mortgage Contract and both Guarantees were all integral parts of this overall operation.

113. This approach fits with the definition of an “investment” in the each of the two applicable BITs:

(1) *Estonia-Finland*: The definition in the Estonia-Finland BIT (Article 1(a)) provides (*inter alia*):

“(i) *movable and immovable property and any other property rights such as mortgages, liens or pledges;*

“(ii) *shares, stocks and debentures of companies or interest in the property of such companies;*” and

*“(iii) title or claim to money or right to any performance having an economic value.”*

(2) *Estonia-Germany*: The definition in the Estonia-Germany BIT (Article 1) provides (*inter alia*):

*“a) ownership of movable and immovable assets, and other material property rights such as mortgages and liens”* and

*“c) claims to money spent to create property holdings, or claims to benefits of economic value.”*

114. The Banks' investment also satisfies the definition meaning of “investment” in Article 25(1) of the ICSID Convention.
115. Moreover, the Banks' original investment was validly made. The validity of the Loan Agreement has not been contested in any legal proceedings. The question whether or not the Payment Agreement and the Mortgage Contract were valid under Estonian law is not relevant to the Tribunal's jurisdiction in these arbitration proceedings.
116. All the actions of the Respondent that form the basis of its liability to the Banks relate to the Loan granted to ESVA and the Guarantee issued by Estrôbprom. Subsequent events, including the Payment Agreement and the Mortgage Contract, all emanate from the prior financing of the ESVA by the Banks, *i.e.* the Banks' original investment. With the Loan and the Guarantee, ESVA was able to build a modern fish-processing factory in Estonia, on the eve of the Respondent's independence. This factory still exists and operates successfully.
117. The annulment of the Payment Agreement and Mortgage Contract and the deletion of the mortgages are incompatible with the requirement of fair and equitable treatment required by the two BITs. This requirement is independent of any possible application of the notion of “denial of justice”. The Banks recognize that it was not the Respondent as a party but RAS Ookean that pursued this annulment in Estonian legal proceedings. However, the Banks contend that these acts should be imputed to the Respondent as it controlled the Ookean bankruptcy estate. Before that bankruptcy, the Respondent had control of Ookean itself as

- well. In that capacity, the Respondent supported Ookean's non-compliance with its obligations under the Estrôbprom guarantee.
118. The liability of the Respondent lies in the overall effect of the Respondent's actions which left the Banks empty handed in November 2001; and the Respondent is responsible for all damages caused by its actions and omissions to the Banks.
119. With regard to damages, the Banks contend that they have manifestly suffered damages, having lost:
- (1) The major part of their original investment;
  - (2) The interest attributable to the investment according to the Loan Agreement;
  - (3) The costs and expenses due to the court proceedings in Estonia, and the additional sum returned to the bankruptcy estate in regard to the "Heinaste"; and
  - (4) The profit that the invested amount would have generated had it been repaid to the Banks in time.
120. Compensation to be awarded to the Banks should be determined on the basis of the general principles of international law, *i.e.* full compensation with interest consisting of unpaid principal, interest and default interest.
121. Interest on the unreturned investment should be calculated either (i) according to the default interest rate identified in the Loan Agreement compounded annually from the Notice of Termination (*i.e.* 16 December 1992) to the Supreme Court decision of 16 November 2001 and at an annually compounded interest of 6% per annum thereafter or (ii) alternatively at an annually compounded interest of 6% per annum from the Notice of Termination.

122. The Respondent took over Estrôbprom – later RAS Ookean – and its assets. Thus, the Respondent also assumed Estrôbprom's liabilities. In this context, the rules on State Succession under international law do not apply.

***(D) The Formal Relief Claimed by the Banks***

123. In their Memorial of 15 July 2004, the Banks requested the Tribunal to decide that:

- (A) The Respondent has breached its obligation to accord, to the investment of the Banks, treatment in accordance with the BITs and international law, including fair and equitable treatment, full protection and security and compliance with commitments made;
- (B) The Respondent has directly or indirectly taken measures tantamount to expropriation or nationalisation of the Banks' investment;
- (C) The Respondent's expropriation or nationalisation of the Banks' investment has been done without due compensation;
- (D) Breaches of the Respondent's obligations, separately or in aggregation, have caused the Banks damage;
- (E) The Respondent shall pay to the Banks:
  - (E1) Monetary damages in the amount of USD 7,159,186.45 and EUR 18,446,031.26 consisting of:
    - the unpaid principal, interest and default interest as at 16 December 1992, according to the Loan Agreement, with the German marks converted to Euros; and
    - default interest on the above in accordance with the Loan Agreement (until 16 November 2001) and at the rate of 6% (after 16 November 2001)

- compounded annually as per 15 July 2004 and with the German marks converted to Euros;
- (E2) Alternatively and as a subsidiary claim, monetary damages in the amount of USD 7,276,207.81 and EUR 10,384,167.38 consisting of
- the unpaid principal, interest and default interest on 16 December 1992, according to the Loan Agreement, with the German marks converted to Euros; and
  - default interest on the above amounts at the rate of 6% compounded annually as per 15 July 2004 and with the German marks converted to Euros;
- (E3) Monetary damages in the amount of USD 622,143.32 and a maximum of EUR 1,200,000.00 due to the expenses of the Banks incurred prior to this Arbitration and the additional sum returned to the estate of RAS Ookean, consisting of:
- the expenses and costs of the Banks before this Arbitration, as per Section VI.3.3 of the Memorial and as specified at a later stage; and
  - the additional amount paid to the bankruptcy estate of RAS Ookean due to the sale of Heinaste as per Section VI.3.5 of the Memorial;
- (E4) Interest on the sums claimed above, at the rate of 6% compounded annually until the date of payment or, alternatively, default interest in accordance with what the Tribunal may consider appropriate;
- (E5) The above sums be made payable to the Banks in equal shares to the Loan, *i.e.* one-third for each Bank within thirty days of the date of the Award;
- (E6) Compensation for all the expenses and fees incurred by the Banks in connection with these arbitration proceedings together with interest; and
- (F) the Respondent shall bear all the expenses and fees of the arbitration proceedings including the fees and expenses payable to the Arbitrators.

## ***PART IV: THE RESPONDENT'S CASE***

### ***(A) Introduction***

124. The Respondent submits first of all that the Tribunal has no jurisdiction in this matter to decide any of the Banks' claims on the merits. There is no "investment" within the meaning of the applicable BITs or under the ICSID Convention. The Loan is not an investment and the Payment Agreement is even less so. Far from contributing any value to the economy of the Respondent, the entire purpose of the Payment Agreement was to extract funds from RAS Ookean and thus from the territory of Estonia.
125. Further, the Payment Agreement does not meet with the criterion that an investment must validly exist. It did not exist validly at the time when the two BITs came into force, as the Estonian Courts held that the Payment Agreement was invalid from its inception. And if the Loan is to be considered as an investment within the meaning of the ICSID Convention or the BITs, it was an investment not in Estonia but in the USSR.
126. The Respondent did not succeed the USSR under international law, nor the Estonian SSR. Estonia did not inherit or otherwise succeed to the public or commercial debts of the USSR or Estonian SSR. There is also no merit to any of the Banks' claims.

### ***(B) The Alleged Facts***

127. According to the Respondent's case, Estrôbprom and its business were part of the old Soviet system implanted on Estonian territory. Estrôbprom was not an independent legal entity: it was a Soviet instrumentality, established in Estonian territory but controlled from Moscow. It was a "socialist state production company", incorporated under Soviet law, under the direct command of the Soviet state organ Zapryba, the "West Basin Fisheries Production Association". It



was also administratively subordinate to Sovrybflot, the All Union Fishing Fleet of the USSR. Both Zapryba and Sovrybflot were instrumentalities of the USSR Fisheries Ministry in Moscow.

128. The existing debt of Estrôbprom did not pass to Estonia, but remained with the USSR (later the Russian Federation), as did all of Estrôbprom's assets located elsewhere in the USSR (such as bank accounts and other receivables). RAS Ookean cannot be regarded as the successor (universal or partial) to Estrôbprom. The Respondent did not assert any rights over Soviet state assets and property located outside Estonian territory, such as monies and other instruments that belonged to the Estonian SSR or USSR state enterprises and organisations formerly based in Estonia. These remained the property of the USSR.
129. The assets (or “means of production”) of Estrôbprom and the units subsumed within it were the property of the state, *i.e.* the USSR. Thus, in late 1989, the USSR, acting through the USSR Fisheries Ministry, leased the “fixed and current assets” of Estrôbprom to the collective of its workers. This was the legal form in which the Respondent found Estrôbprom at the restoration of Estonian independence in August 1991. With such independence, the assets possessed and managed by Estrôbprom devolved to the Respondent.
130. RAS Ookean had no assets of its own. The assets contributed to RAS Ookean, as for all such companies, remained the property of the Respondent: the company was only the “possessor” of these assets. An annex to the Articles of Association of RAS Ookean set out the state property placed under the management and possession of RAS Ookean. This annex did not make reference to shares in ESVA and, accordingly, no shareholding in ESVA was ever recorded in the company's balance sheet. Even under Soviet rule, Estrôbprom comprised different structural units, such as a fishing port and other distinct entities, two marine schools and a fish factory in Pärnu. Accordingly, when in August 1990 Zapryba had requested the local Estonian authorities to register the “Lease Association Estrôbprom”, it also requested separate registrations for the discrete units within it, *i.e.* the two marine schools, the fish factory and the repair shipyard.

131. The Articles of Association of RAS Ookean also made clear that the state was not responsible for the company's liabilities.
132. After the Respondent's independence in August 1991, Estrõbprom experienced great economic problems, lacking access to fishing grounds through Soviet fishing quotas. The main cause of ESVA's and Ookean's bankruptcy was the dissolution of the USSR. The business of these companies was based on the assumption that raw materials for the production of fish products would be supplied at low prices (in domestic currency) from the USSR and other countries, while the fish products could primarily be sold to western markets for valuable foreign exchange. By 1992, it was no longer possible to obtain such cheap raw material. As a consequence of these significant economic changes, the reduction in income could not service these companies' burden of debt.
133. RAS Ookean's chances of survival in an independent Estonia with 1.5 million inhabitants were always poor, the company having been plagued by structural problems from the outset. On the one hand, Estonia's needs were vastly disproportionate to the unwieldy organisation that was RAS Ookean. On the other hand, RAS Ookean (and before it, RE Ookean) was unable meaningfully (still less, profitably) to employ its fishing fleet. RAS Ookean's problems were compounded by the inexperience of its management and entrenched Soviet-era traditions.
134. The Respondent's independent auditors (the State Audit Office) performed a separate audit of RAS Ookean as a whole (*i.e.*, not only the company's accounts), and their report dated July 1994, was scathing. It was noted that that Mr [REDACTED] with a few advisors had developed a "development plan" based on the idea that RAS Ookean would "reincorporate the [fishing] port [of] Kopli into [its] composition", but this plan was "focused on unsubstantiated prognostication, [unsupported] by a reliable frame of reference and concrete economic calculations". Finally, the State Audit Office identified several irregularities, including failures to comply with various regulations on the disposal of proceeds of State property.

135. Through the Loan of FIM 93 million, ESVA was heavily over-extended. The Banks had made a mistake by over-leveraging ESVA and not factoring into their calculations the possibility that the artificially cheap raw materials provided by the USSR might cease to be available to ESVA. These were commercial risks; it is not contended that the Respondent was in any way responsible for them. Estrôbprom was totally unsuited to post-independence realities or to a free market economy. In that sense, it was essentially destined to fail.
136. However, the Banks had made another, more elementary mistake. Under Soviet law, only the USSR Fisheries Ministry could provide a Guarantee, as distinct from its subordinate entities such as Estrôbprom. This may well have been known to the Banks earlier, but it was proved by RAS Ookean during the court proceedings commenced by the Banks in February 1993.
137. The Banks today contend that they “based their decisions to grant the Loan and accept the Guarantees, to a large extent, on the information provided on [Estrôbprom's] assets”. The Respondent has no way of knowing what the cautious phrase “to a large extent” means. The record suggests that the Banks' due diligence was limited to a manifestly summary description of Estrôbprom, which was entitled “Company Background” and does not appear to have been created for the purposes of the ESVA transaction or the Loan: it nowhere records that it is provided so that the Banks could rely on it for any purpose; and it was moreover provided by Estrôbprom's Director-General and not by one of its independent advisors or auditors.
138. The Respondent relieved Estrôbprom of several uncommercial assets, which were burdensome and did not form part of its core activity, namely fishing. These were Estrôbprom's fishing port, two marine schools and the fish factory in the city of Pärnu, all of which were transferred to state institutions in late 1991 and early 1992. Even though that burden was lightened and despite other measures that its management was able to take (principally to enter joint-venture agreements abroad and permitting the company to put to use some of its trawlers), Estrôbprom was in a hopeless position.

139. The Respondent acknowledges that numerous negotiations took place with the Banks in order to solve the problem of the unpaid Loan. However, in no way did the Respondent commit itself to a repayment of the Loan, or more specifically, to that part of the Loan that was guaranteed by Estrôbprom. When the Loan was negotiated, the Banks initially required guarantees from the USSR Ministry of Fishery or the Council of Ministers of the ESSR for 52% of the debt. This is not what the Banks received: they received only a guarantee from Estrôbprom.
140. On the advice of Mr [REDACTED] an advisor to Mr [REDACTED] (Ookean's Chairman of the Board), Ookean accepted Mr [REDACTED] idea and approved in principle an agreement whereby six Moonsund-class trawlers would be sold and part of the proceeds would be paid over to the Banks. In return, RE Ookean would obtain 52% in "New ESVA", a company that would acquire ESVA's assets and in which RE Ookean would be a founding shareholder. After the 52% acquisition, RE Ookean would acquire the remaining 48% from Valio, for USD 5 million.
141. Mr [REDACTED] had also secured the support of Mr [REDACTED] the Estonian Minister of Economy. In early April 1993 Mr [REDACTED] tabled before the Estonian Cabinet a proposal for a Government Order permitting "the state-owned company 'Ookean' to sell six 'Moonsund'-type trawlers to foreign companies", thereby freeing Mr [REDACTED] hands in the negotiations. But the Estonian Government did not endorse this proposal. Instead, on 13 April 1993 it was decided to "agree in principle" with the proposal of the Estonian Ministry of Economy to start negotiations regarding the sale of factory-trawlers of Ookean, without taking binding decisions.
142. Ultimately, RAS Ookean entered into the Payment Agreement in September 1993, and it did so in order to obtain a participation in ESVA. The Banks had assured RAS Ookean that it could participate in the new ESVA (*i.e.* Paljassaare). However, the Banks then did everything to prevent RAS Ookean from participation. The Banks transferred all of ESVA's estate (but not its debts) to Paljassaare for a fraction of its value, an ostensible payment by interest-free bonds spread over eight years.

143. For its part, RAS Ookean complied with the Payment Agreement, by selling one of the six vessels in February 1995. It also obtained permission from the Estonian Ministry of Economy to comply with the Payment Agreement. The Banks' conduct caused RAS Ookean to invalidate the Payment Agreement. As already explained, in consideration for agreeing to make payment to the Banks under the Payment Agreement, RAS Ookean was (according to Article V) to obtain from the Banks their rights to the bankruptcy estate of ESVA, proportionately to the payments RAS Ookean would make to the Banks. This was so, even though RAS Ookean had discovered that the Banks and Valio had emptied ESVA of all value, thereby rendering the Payment Agreement worthless for RAS Ookean.
144. The Banks, for their part, failed to uphold their end of the bargain with RAS Ookean.
145. The terms of the Payment Agreement are, in themselves, unremarkable. Consistent with the factual background that led to its conclusion, there is nothing to suggest that this was anything other than an arm's length agreement with a purely commercial objective, namely to permit RAS Ookean to become the new majority shareholder in ESVA. Nowhere does the Respondent appear as a party to the Payment Agreement.
146. The parties were the Banks and RAS Ookean, whose published Articles of Association left no doubt that it was “responsible” for its liabilities to the extent of property in its ownership; that the Respondent was not responsible for the company's liabilities; and that the company was not responsible for the Respondent’s liabilities.
147. The terms of the Payment Agreement, drafted by the Banks, reveal no governmental purpose, and require no exercise of governmental authority on the part of RAS Ookean (even assuming that RAS Ookean might have had any such authority, which it did not). To the contrary, the Payment Agreement was a straightforward commercial contract by which RAS Ookean “undertakes to repay to the Banks the ESVA loan” by selling six nominated ships by the end of 1997; and, in return, the Banks (a) agreed to permit RAS Ookean to participate in

- meetings of the creditors of ESVA and (b) undertake to “transfer their rights and obligations in the bankruptcy estate of ESVA”... “on [a] pro rata basis in proportion to the repaid principal amounts [of the ESVA Loan]”.
148. Article IX(5) of the Payment Agreement removes any possible doubt on the commercial character of the transaction. There, RAS Ookean “acknowledges and agrees that the transaction described herein is commercial in nature rather than governmental or public” and waives any possible form of immunity from jurisdiction or execution.
149. The Payment Agreement was not entered into at the request of the Respondent, or by the Respondent itself, acting through RAS Ookean as its surrogate. The Banks attempted, and failed, to get a promise or guarantee from the Respondent to pay the monies claimed by the Banks; and they settled instead for a promise from RAS Ookean. The Respondent would never have abandoned a fundamental tenet of its independence not to assume Soviet debt, whether by issuing a state guarantee or otherwise; and such Soviet debt included Estrôbprom debt.
150. By its express terms, the Minister's letter (*i.e.* the ██████ Letter) did not create any liability on the Respondent's part; indeed, that is precisely what the Banks attempted to procure but failed to acquire from the Respondent. Instead, the Banks received an unofficial letter merely expressing an intention not to interfere in any lawful transaction RAS Ookean might agree with the Banks; and indeed the Respondent did not interfere. The ██████ Letter was not on its face a commitment letter and could not have been treated as a commitment letter for several fundamental reasons that Mr ██████ RAS Ookean, the Banks and their advisors knew well at the time. The stated purpose of the letter was solely to “help you [the Banks] assess the merits” of the Payment Agreement. Such general and non-committal wording is routinely found in comfort letters issued in connection with such transactions. This is entirely consistent with the opening line: “Please be advised that we are aware and in support of the above agreement”.

151. The [REDACTED] Letter was undoubtedly prepared by the Banks themselves, rather than the Ministry of Economy (or the Minister himself). It follows in structure and general content the Banks' suggestions in a meeting with RAS Ookean's negotiators (led by Mr [REDACTED] in July 1993. No government official attended that meeting; and there is no evidence that the Banks later showed any interest in having the [REDACTED] Letter issued through the established procedures within the Ministry of Economy. Also a comparison between certain drafts of the [REDACTED] Letter proves that its terms were negotiated exclusively between the Banks and RAS Ookean, not with the Respondent.
152. To read the [REDACTED] Letter in a more extensive way, as the Banks now seek to do, would be tantamount to changing its terms with retrospective effect, to give the Banks a legal “commitment” or “warranty” that the Respondent manifestly never gave or agreed to give. Essentially, the Banks are asking the Tribunal to re-write history by transforming the [REDACTED] Letter into the government guarantee that the Banks say they initially sought – and manifestly failed – to obtain from the Respondent.
153. Moreover, the Banks' reading would make the [REDACTED] Letter patently illegal. Yet, breaching the law is not what a Minister would have set out to do, or what the Banks or their advisors could reasonably assume that he had done. The law was clear to all concerned and set out in Article 65(10) of the Estonian Constitution and implementing regulations. It was to the effect that the instruments by which the Estonian Republic, in exceptional cases, undertook binding financial commitments were official letters made on a specific express authorisation in the form of a Government Order. The [REDACTED] Letter was neither official nor authorised, as the Banks knew.
154. In the early spring of 1995, RAS Ookean warned the Banks (and Paljassaare) that it would have to consider taking legal action to protect itself against their actions. At the same time, it proposed to the Banks a generous settlement, under which the Banks would be paid USD 8.7million in 1995; and, as Mr [REDACTED] put it, “keep Paljassaare for themselves”. The Banks ignored both RAS Ookean's warnings and its proposal. Mr [REDACTED] explained that at the end of August 1995, he asked the

- Banks to give an immediate and final response to RAS Ookean's proposals, which had been discussed for five months. But the Banks failed to give any response at all. By that time, RAS Ookean's illiquidity had become critical; and creditors were attacking it from all sides, seizing several of its assets. At the time when RAS Ookean resorted to the Estonian Courts against the Banks, as the Payment Agreement expressly authorised it to do, a major creditor applied for the company to be put in bankruptcy; and RAS Ookean was in no position to resist this application.
155. The Respondent notes that, indeed, there was a delay in the sale and mortgaging of the six vessels. Eventually, however, when RAS Ookean was in the process of selling the “Heinaste”, it learned that the Banks had no intention of honouring the Payment Agreement or of granting any shareholding interest in the new ESVA – *i.e.* the Banks' rights to the bankruptcy estate of ESVA, proportionately to the payments RAS Ookean would make to the Banks under the Payment Agreement. The Banks delayed the negotiations. A revised draft shareholders' agreement was prepared by the Banks only at the end of June 1994. The Banks' new draft was unsatisfactory to RAS Ookean, principally because it did not provide that the company would become a shareholder in Paljassaare.
156. Meanwhile, however, the Banks and Valio had agreed to acquire ESVA's assets for a fraction of their value. Thus, RAS Ookean no longer stood to gain anything from the Payment Agreement. Nevertheless, RAS Ookean continued to comply with the Payment Agreement, including the sale of the “Heinaste”.
157. From early onwards in the spring of 1995, RAS Ookean's legal representative, Mr [REDACTED] took steps to protect RAS Ookean's rights, which he set out in detail in his written witness statement. In essence, Mr [REDACTED] adopted a twin strategy, warning from the outset that if no satisfactory settlement were reached, RAS Ookean would take legal action to protect its rights: (i) on the one hand, RAS Ookean explained to the Banks and Paljassaare that their actions were in breach of the Parties' understandings since 1993, and that RAS Ookean ought to be permitted to participate as a shareholder in Paljassaare; and (ii) on the other, RAS Ookean offered to pay to the Banks the sum of USD 6 million (to be obtained by



- selling three vessels), payable in 1995 and in addition to the “Heinaste's” proceeds, to settle the matter without further risks and costs of litigation.
158. RAS Ookean's calls to be granted a participation in Paljassaare were ignored by the Banks. As to its settlement proposals, the Banks purported to question their feasibility and, once more, dragged this matter out for five months by engaging in desultory correspondence. On 30 August 1995, Mr ██████ asked the Banks to take a final position on RAS Ookean's proposal. They did not do so. The Banks' recalcitrance, coupled with RAS Ookean's severe liquidity problems and threat of imminent bankruptcy, left RAS Ookean no other realistic choice but to initiate legal proceedings to resolve the dispute.
159. Mr ██████ study of the Payment Agreement had led him to the conclusion that the Payment Agreement was invalid for the following principal reasons: (i) Mr ██████ lacked authority to sign the Payment Agreement, given that the Board had authorised the signing of a “loan agreement”, while the Payment Agreement could not be regarded, in Mr ██████ view, as an agreement for a loan; and (ii) the Articles of Association of RAS Ookean were to be read strictly and did not provide that the company could underwrite the debts of a third party, that is, to undertake to repay ESVA's debt by concluding the Payment Agreement.
160. Mr ██████ did not consider that the Payment Agreement was binding on RAS Ookean on any other basis, including Ookean's status as successor to Estrôbprom. He does not appear to have considered the relevance of the Respondent's stated policy not to accept any Soviet debt (including that of Estrôbprom under the Guarantee), or the impact of the invalidity of the original Guarantee under Soviet law.
161. On 20 October 1995, RAS Ookean filed an action seeking a declaration of invalidity of the Payment Agreement (and, shortly thereafter, the Mortgage Contract too). As Mr ██████ explains, RAS Ookean's action coincided with an application by the Port of Tallinn that RAS Ookean be placed in bankruptcy. The application of the Port of Tallinn surely came as no surprise to all involved (including the Banks). An application by an employee on account of unpaid

wages had been pending since August 1995, while RAS Ookean had already fended off other similar applications in the preceding months. As described in more detail below, RAS Ookean was by now in a hopeless financial position; and independent audits confirmed that it had been insolvent for months before October 1995. In short, RAS Ookean's position was irredeemable. For these objective reasons, it was in no position to object to an application for bankruptcy, a possibility that the Board had predicted as most likely to materialise since September 1995. RAS Ookean's bankruptcy was inevitable.

162. In conclusion, during 1995, RAS Ookean was being attacked from all quarters by creditors. By 23 October 1995, RAS Ookean was in no position to oppose bankruptcy proceedings: its insolvency was clear, not being limited to temporary illiquidity. On this basis, it was declared bankrupt by the Tallinn City Court on 30 October 1995. The Court appointed two temporary trustees (Messrs [REDACTED], both practising professional lawyers) and an assistant trustee (Mr [REDACTED] who were later confirmed by the committee of the creditors. Under Estonian law, trustees in bankruptcy are not considered to exercise judicial functions; indeed, judges can never serve as trustees in bankruptcy; and the decisions of such trustees are subject to scrutiny by the committee of creditors and, ultimately, the Courts, which can both dismiss them.
  
163. Four distinct cases (or sets of cases) were litigated in the Estonian Courts by RAS Ookean's trustees in bankruptcy:
  - (a) The proceedings on the Payment Agreement and the Mortgage Contract;
  - (b) The proceedings on the discharge of the mortgages (or pledges, as described by the Respondent);
  - (c) The proceedings to admit the Banks as creditors in RAS Ookean's estate;  
and
  - (d) The proceedings to recover property of RAS Ookean.

***(C) The Alleged Breaches of the BITs***

164. Neither under international law nor in fact is there any breach of either of the BITs. This dispute is limited to a commercial dispute between the Banks and RAS Ookean. The Payment Agreement had a commercial character: it was an arm's length agreement with a purely commercial objective, namely to permit RAS Ookean to become majority shareholder in the new ESVA. The Respondent was not a party to the Payment Agreement.
165. With regard to the damages claimed by the Banks, the Respondent contends that these figures are wildly exaggerated. The Banks have sustained no compensatable loss; and to the extent that there is any loss at all, it has resulted from the Banks' own choices and their failure to provide proof in the proper form to the Estonian Courts.

***(D) The Formal Relief Claimed by the Respondent***

166. The Respondent's primary submission is that the Banks' claims all fall outside the jurisdiction of this Tribunal under Article 25(1) of the ICSID Convention and the two BITs. In its Opening Statement at the Hearing, the Respondent also submitted that the claim of the Second Claimant was outside the Tribunal's jurisdiction *ratione temporis* because the relevant BIT (the Estonia-Germany BIT) entered into force only in 1997 and the events on which the Banks relied took place before such entry into force<sup>10</sup>.
167. In its Counter-Memorial of 17 November 2004, the Respondent also requested that the Tribunal:
- (1) Dismiss all of the Banks' claims in their entirety; and
  - (2) Order the Banks to pay all of the costs and expenses of this arbitration, including the fees and expenses of the Tribunal, the fees and expenses of

---

<sup>10</sup> Transcript p. 200.

any experts appointed by the Tribunal and the Respondent, the fees and expenses of the Respondent's legal representation in respect of this arbitration, and any other costs of this arbitration.

***PART V: THE ISSUES TO BE DECIDED BY THE TRIBUNAL***

168. As determined by the Tribunal, the issues to be decided by this Tribunal in this Award are the following:

***Issue 1:*** Does this Tribunal have any jurisdiction over any of the claims advanced by any of the three Banks?

(This issue is addressed in Part VI of this Award).

***Issue 2:*** If so, has any breach of either of the relevant BITs been established by the Banks?

(This issue is addressed in Part VII of this Award).

***Issue 3:*** If so, is liability for such breach counterbalanced by any misconduct by the Banks, as contended by the Respondent?

(This issue is addressed in Part VIII of this Award).

***Issue 4:*** If not, what damages and interest (if any) should be awarded to the Banks in respect of any liability for breach of the applicable BITs?

(This issue is addressed in Part IX of this Award).

169. It is now appropriate to address below each of these issues in turn, as indicated, in Parts VI to IX of this Award. The separate question of legal and arbitration costs is considered in Part X of this Award.

## ***PART VI: ISSUE 1 – JURISDICTION***

### ***(A) Introduction***

170. Where a claim is brought by an investor under a BIT and as claimant seeks to establish jurisdiction under the ICSID Convention over the respondent host state, an arbitral tribunal must satisfy itself that the relevant investment falls within the definition of “investment” *both* within that BIT and within Article 25(1) of the ICSID Convention. In these ICSID arbitration proceedings, the Banks assert such jurisdiction, which the Respondent challenges. It is appropriate to begin with the two BITs and then to consider Article 25(1) of the ICSID Convention.

### ***(B) The Two BITs***

171. The Tribunal here first analyses the question whether the “investment” alleged by the Banks falls within the definition of the two applicable BITs.
172. *Estonia-Finland BIT*: The Government of the Republic of Estonia and the Government of the Republic of Finland signed on 13 February 1992 the Estonia-Finland BIT. It entered into force on 2 December 1992.
173. Article 8(1)(a) and (b) of this BIT reads as follows, as regards investor-state arbitration:<sup>11</sup>

*“(1) Any legal dispute between an investor of one Contracting Party and other Contracting Party concerning an investment of the former in the territory of the latter which has not been amicably settled during three months from written notification of a claim may, at the request of either Party to the dispute, be submitted either to:*

- (a) the International Centre for Settlement of Investment Disputes (hereinafter called "the Centre") having regard to the applicable provisions of the Convention on the Settlement of Investment Disputes between States and Nationals of other States opened for signature at Washington D.C. on 18 March 1965, in the event both Contracting Parties shall have become party to this Convention;... ”*

---

<sup>11</sup> Articles 8(2) and (3) are not relevant for the present dispute.

174. *Estonia-Germany BIT*: The Republic of Estonia and the Federal Republic of Germany signed on 12 November 1992 the Estonia-Germany BIT. It entered into force on 12 January 1997.

175. Article 11 of this BIT reads as follows (translated from German), as regards investor-state arbitration:

*“(1) Investment-related disputes between one Contracting Party and the citizens or companies of the other Contracting Party shall if possible be settled amicably between the parties to the dispute.*

*(2) If a dispute is not settled within six (6) months from the point of time at which settlement was demanded by one of the parties to the dispute, it shall, at the request of the citizen or the company of the other Contracting Party, be subjected to arbitration. If the parties to the dispute do not agree otherwise, the provisions of Article 10, Section 3 to 5, apply in that the members of the court of arbitration, as specified in Article 10, Section 3, shall be appointed by the parties to the dispute. Furthermore, if the time-limits referred to in Article 10, Section 3, are not adhered to and no other solution has been reached, each party to the dispute shall be entitled to turn for the necessary appointments to the President of the Court of Arbitration of the International Chamber of Commerce in Paris. Arbitral awards are enforced according to intrastate law.*

*(3) [...]*

*(4) If both Contracting Parties have entered into the Convention on the Settlement of Investment Disputes between States and Citizens of Other States, of 18 March 1965, disputes existing between the parties as specified under this Article shall be subjected to arbitration within the above Convention, unless the parties to the dispute agree otherwise. Both Contracting Parties declare hereby their approval of such a procedure.”*

176. In this case, the issue whether there is an investment under these two BITs raises four separate questions: (i) Was there any investment at all? (ii) If so, was this investment made in Estonia? (iii) Does the definition of such an investment apply to investments made before the respective dates of the two BITs' entry into force? and (iv) Was such investment validly made, within the meaning of the two BITs? It is appropriate to consider each question in turn.

**(i) Was there any Investment at all?**

177. Article 1(a) of the Estonia-Finland BIT provides:

*"investment" means every kind of asset connected with economic activities and in particular, though not exclusively, includes:*

- (1) movable and immovable property and any other property rights such as mortgages, liens or pledges;*
- (2) shares, stocks and debentures of companies or interest in the property of such companies;*
- (3) title or claim to money or right to any performance having an economic value;*
- (4) copyrights, industrial property rights (such as patents, trade marks, industrial designs) technical processes, know-how, business names and goodwill;*
- (5) business concessions conferred by law or under contract, including concessions to search for cultivate extract or exploit natural resources."*

178. Article 1 of the Estonia-Germany BIT provides:

*"For the purposes of this Agreement*

*The expression "Investments" has the meaning of property holdings of any type, especially, however, of :*

*[a] ownership of movable and immovable assets, and other material property rights such as mortgages and liens;*

*[b] shares in companies and any other types of holdings;*

*[c] claims to money spent to create property holdings, or claims to benefits of economic value;*

*[4] intellectual property rights, such as copyrights, patents, utility models, commercial designs and models, marks, trademarks, business secrets and company secrets, technical applications, know-how and goodwill;*

*[5] licenses under public law, including search and utilization licenses.*

*Changes in the type of an investment do not in any way affect the nature of the asset as an investment."*

179. In the Tribunal's opinion, the rights enjoyed by the Banks qualify as an "investment" within the meaning of these broad definitions, subject to other



questions considered below. The investment includes the rights and obligations under the Loan Agreement with its associated Guarantees, all related to the original financing of the ESVA joint venture, as continued thereafter. Under the Estonia-Finland BIT, these rights and obligations constitute a "...kind of asset connected with economic activities...". These rights and obligations would also qualify as an investment in the light of the more specific provisions of Article 1(a)(i) and (iii) of the Estonia-Finland BIT. Under the Estonia-Germany BIT, these rights and obligations likewise qualify in the light of the (non-exclusive) general description. It is also significant that the recitals to the two BITs suggest a broader interpretation of all these concepts: both refer to the desire to intensify the economic cooperation of the two countries beyond August 1991. There can be no doubt that the Banks' continued funding of the ESVA joint venture was an act of economic cooperation with the Respondent.

180. The Banks have submitted that these rights and obligations should not be considered on a "stand alone basis" but as a "whole". Nonetheless, even assuming this approach to be incorrect, the Loan Agreement qualifies as an investment under the BITs both on a stand alone basis in 1989 and on the basis of all other factors from 1989 onwards to 2001. For the Loan itself, this is in fact expressly acknowledged by the Respondent.
181. Accordingly, the Tribunal answers this first question in the affirmative, in favour of the Banks' case.

***(ii) Was this Investment made in Estonia?***

182. Although the original investment was made by the Banks in Estonian territory then comprising part of the USSR and not the Republic of Estonia, it was nonetheless made in such territory in 1989 and continued beyond August 1991 in Estonia.
183. Accordingly, the second question whether there was an investment in Estonia for the purposes of the Estonia-Finland and Estonia-Germany BIT is answered in the

affirmative by the Tribunal, in favour of the Banks" case. (The answer to this question also overlaps with the third question below).

***(iii) Does the Definition of such an investment apply to investments made before the BITs' entry into force?***

184. The third question is whether the definition of an "investment" in either BIT applies to any investment made or continued before that BIT"s entry into force.

185. Article 2(2) of the Estonia-Finland BIT reads as follows:

*"(2) Subject to the provisions of paragraph (1) of this Article, this Agreement shall apply to all investments made in the territory of a Contracting Party by investors of the other Contracting Party before or after the entry into force of this Agreement."*

186. Article 9 Estonia-Germany BIT reads as follows:

*"This Agreement applies also to investments made by citizens or companies of one Contracting Party before this Agreement in the territory of the other Contracting Party in accordance with its legal regulations."*

187. Thus, both definitions in the two BITs have retroactive effect to this extent, qualifying, as a covered investment, an investment made in the "territory" of the Respondent before the coming into force of the BITs, even at a time before Estonian independence from the USSR in August 1991.

***(iv) The Validity of the Banks' Investment***

188. Both BITs require the investment to be made in accordance with the laws and regulations of the host country: see Article 2 of the Estonia-Finland BIT and Article 2 of the Estonia-Germany BIT.

189. In the present case, the decisive issue is the original character of the investment. As described earlier, the Loan and the Loan Agreement were the Banks' original investment. It is not disputed that both were made in accordance with the law and regulations then prevailing in Estonian territory. It is contended by the Respondent that the Guarantees attached to the Loan were invalid but, even if this were so at that time, that could not by itself invalidate the legality or other validity of the Loan and the Loan Agreement, *i.e.* the substance of the Banks' original investment.
190. The later Payment Agreement cannot change the character of that investment. Accordingly, the fact that the Payment Agreement was eventually declared invalid by the Estonian Supreme Court cannot here decide the Tribunal's jurisdiction. That decision, for present purposes, leaves intact the Banks' investment, *i.e.* the Loan Agreement and the Loan as originally made in 1989 and continued by the Banks thereafter.

***(C) Can the Estonia-Germany BIT Apply to the Second Claimant's Claims?***

191. As regards the Estonia-Germany BIT, the issue is whether any of the Second Claimant's claims arise before the date of the Respondent's obligations under that BIT.
192. The Respondent contends that the Tribunal has no jurisdiction over the Second Claimant's Claims, *ratione temporis*, because the alleged breaches of the Estonia-Germany BIT took place before that BIT entered into force on 12 January 1997. It submits that this BIT has no retroactive effect as regards the Respondent's obligations assumed under the BIT; and it cannot therefore apply to any alleged breach occurring prior to its entry into force in 1997. It will be recalled that many events invoked by the Second Claimant pre-date January 1997, principally the Payment Agreement of 17 September 1993, the [REDACTED] Letter also of 17 September 1993 and the Mortgage Contract of 4 March 1994.

193. In short, the Tribunal accepts the Respondent's general approach as regards the non-retroactive effect of the Estonia-Germany BIT. Under international law, the basic rule on the non-retroactivity of treaties is expressed in Article 28 of the 1969 Vienna Convention on the Law of Treaties. It provides: "*Unless a different intention appears from the treaty or is otherwise established, its provisions do not bind a party in relation to any act or fact which took place or any situation which ceased to exist before the date of entry into force of the treaty with respect to that party.*" Similarly, Article 13 of the International Law Commission's Articles on State Responsibility provides: "*An act of a State does not constitute a breach of an international obligation unless the State is bound by the obligation in question at the time it occurs.*" It follows that, pursuant to Article 28 of the Vienna Convention and subject to the existence of a continuing breach (as discussed below), the Estonia-Germany BIT does not bind the Respondent as regards that BIT's substantive obligations in relation to any relevant act which took place or any situation which ceased to exist before the date of this BIT's entry into force, namely 12 January 1997.
194. So far as concerns a continuing breach, Article 14(2) of the ILC's Articles on State Responsibility provides: "*The breach of an international obligation by an act of a State having a continuing character extends over the entire period during which the act continues and remains not in conformity with the international obligation.*" In other words, in order to acquire this continuing character the alleged continuing breach must be (i) continuing and (ii) uninterrupted. It is of course necessary to distinguish also between breaches that are continuing in nature and breaches that are not continuing but have effects that continue in time; but this question does not arise on the facts of the present case.
195. As considered below in this Award, the Tribunal considers that the Republic of Estonia violated the Estonia-Finland BIT and the Estonia-Germany BIT. Those breaches were of a continuing character extending beyond 12 January 1997. RAS Ookean, in October 1995, filed its petition to the Tallinn City Court in order to invalidate the Payment Agreement and the Mortgage Contract; and these legal proceedings led eventually to the Estonian Supreme Court's judgment on such

invalidity on 16 November 2001. This extensive litigation, for reasons described below, constitutes a breach by the Respondent of its obligations under both BITs; and as regards the Estonia-Germany BIT that breach continued, uninterrupted, from 12 January 1997 to November 2001, *i.e.* after the entry into force of the Estonia-Germany BIT.

196. Accordingly, to this extent only, the Tribunal decides that it has jurisdiction with regard to the Second Claimant's claims under the Estonia-Germany BIT.

***(D) Article 25(1) of the ICSID Convention***

197. Accordingly, the Tribunal answers in the affirmative the question whether it has jurisdiction under the two BITs to decide the Banks' relevant claims. The next question is whether the Tribunal has any jurisdiction to do so in the light of the ICSID Convention.

198. According to Article 25 (1) of the ICSID Convention, the jurisdiction of the International Centre for Settlement of Investment Disputes:

*"[...] shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally."*

199. Estonia is a Contracting State to the ICSID Convention as of 23 July 1992, Finland as of 8 February 1969 and Germany as of 18 May 1969. The Banks, as "Investors", are and remain nationals of Finland and Germany.

200. The Banks have given their consent to submitting the present dispute between the Parties to ICSID by their Request for Arbitration. It is not disputed by any Party that the dispute between them is a legal dispute; and obviously, that dispute between the Parties arises directly out of the Banks' "investment", as determined above by the Tribunal under the two BITs.

201. The answer to the Tribunal's jurisdiction under the two BITs does not, by itself, suffice for the different question whether or not there was also an “investment” for the purpose of Article 25 (1) of the ICSID Convention. The Banks must satisfy the jurisdictional requirements of both the relevant BITs and the ICSID Convention.
202. As is well known, there is no definition of the term “investment” in the ICSID Convention, as the result of an express decision on the part of those negotiating the terms of the Convention; and there remain grave practical difficulties in identifying the outer boundaries of any definition.<sup>12</sup> It cannot be assumed that the interpretation of this undefined term in the ICSID Convention should necessarily be the same under international law as the defined terms in the two BITs (although it appears from the history of the Convention that the parties' agreement that a dispute is an “investment” dispute will be given certain weight in any determination of ICSID’s jurisdiction<sup>13</sup>).
203. In recent years, the typical features of an investment falling within Article 25(1) of the ICSID Convention have been identified in several decisions of ICSID arbitration tribunals. These features include duration, regularity of profit and return, risk, the size of the investment and its significance in regard to the economic development of the host State. Several ICSID tribunals have also emphasised that it is necessary to look at the overall transaction at issue in the particular case.
204. Thus, in the *CSOB v. Slovak Republic* case<sup>14</sup>, which also concerned a loan agreement, the arbitration tribunal decided:

*“An investment is frequently a rather complex operation, composed of various interrelated transactions, each element of which, standing alone, might not in all cases qualify as an investment. Hence, a dispute that is brought before the Centre must be deemed to arise directly out of an investment even when it is based on a transaction which, standing alone, would not qualify as an investment under the*

---

<sup>12</sup> Christoph H. Schreuer, *The ICSID Convention: A Commentary* (2001), pp 121 and 140.

<sup>13</sup> Aron Broches, "The Convention on The Settlement of Investment Disputes: Some Observations on Jurisdiction," *Columbia Journal of Transnational Law*, Vol. 5, 1966, 261-280, at 268.

<sup>14</sup> *Ceskoslovenska obchodni banka, a.s. v. Slovak Republic* (ICSID Case No. ARB/97/4), Decision on Jurisdiction of 24 May 1999, Exhibit R-114 at para. 72.

*Convention, provided that the particular transaction forms an integral part of an overall operation that qualifies as an investment.”*

In that case, the respondent based its argument (in part) on the fact that CSOB's loan did not cause any funds to be moved or transferred from CSOB to the Slovak Collection Company in the territory of the Slovak Republic. It argued that an investment requires the expenditure of resources by one party (the investor) in the territory of a foreign country (the host State).

205. No such argument arises in the present case. It is common ground that funds representing the Loan were transferred to Estonian territory (albeit then the Estonian Soviet Socialist Republic, as part of the USSR) for the benefit of legal persons in the territory of Estonia, namely ESVA and, later, Estrôbprom.
206. The Tribunal also notes the tests which were applied by other ICSID tribunals when deciding whether an investment in dispute would qualify as an investment under the ICSID Convention. Following the *CSOB* case, the tribunal in *Salini v. Morocco*<sup>15</sup> decided that relevant criteria would include a contribution of a certain duration and participation in the risks of the transaction (which would be the “normal” commercial risks<sup>16</sup>) and the contribution to the economic development of the host state. The investment in the present case would certainly meet with those criteria<sup>17</sup>.
207. It would be possible to extend this survey considerably, including the recent ICSID award of 17 May 2007 in *Malaysian Historical Salvors v. Malaysia*<sup>18</sup>. In the Tribunal’s view, it is not necessary to do so.
208. Applying the general approach described above to the present case, the “overall operation” can readily be identified as the funding of a new fish-processing

---

<sup>15</sup> *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco* (ICSID Case No. ARB/00/4), Decision on Jurisdiction of 23 July 2001, available at <http://ita.law.uvic.ca>, para. 52. See also *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan* (ICSID Case No. ARB/03/29) Decision on Jurisdiction of 14 November 2005, available at <http://ita.law.uvic.ca/>, para 130 et seq., where this test was applied.

<sup>16</sup> Or, as it was stated in *Bayindir v. Pakistan*, para 130: “operational risks”.

<sup>17</sup> The Tribunal notes that it was not materially contested by the Respondent that the Banks' financing of the ESVA plant was a significant contribution to economic development in Estonian territory.

<sup>18</sup> *Malaysian Historical Salvors, SDN, BHD v. Malaysia* (ICSID Case No. ARB/05/10) Award on Jurisdiction of 17 May 2007. This ICSID award was made under the Malaysia-UK BIT (which entered into force on 21 October 1998). It contains a comprehensive survey of legal materials to date on the meaning of “investment” under Article 25 of the ICSID Convention: see para 54 *et seq.*

factory in Tallinn, on Estonian territory, to a total value of approximately USD 25 million, with access (at that time) to cheap and plentiful Soviet-caught fish and a sales and export operation from the USSR to Western markets. Whilst individual parts of that overall operation, *e.g.* the two Guarantees, might not by themselves qualify as an “investment”, the Tribunal considers that overall, there was here a covered “investment” within the meaning of Article 25(1) of the ICSID Convention. Moreover, as already noted above, the Respondent (rightly) concedes that the Loan, by itself, “might even arguably be an investment for ICSID Convention purposes”<sup>19</sup>. Taken together with the Loan Agreement and (if necessary) the Guarantees, the Tribunal considers that the Loan, as the principal part of the overall operation, qualifies as an “investment” under Article 25(1) of the ICSID Convention; and that the “investment” remained as such up to and including the commencement of these arbitration proceedings.

209. Accordingly, for these reasons, the Tribunal determines that it has jurisdiction under the ICSID Convention (and hence jurisdiction) to decide the Banks’ relevant Claims in these arbitration proceedings.

---

<sup>19</sup> Transcript p. 91 and 98.



***PART VII: ISSUE 2 - WAS THERE A BREACH OF THE BITS?***

***(A) Introduction***

210. In their Opening Statement at the Hearing, the Banks summarised the factual grounds in support of their allegations that the Respondent committed breaches of the BITS, as follows:
- (1) The exhaustion of Estrôbprom's assets after its nationalisation by the Respondent;
  - (2) The non-compliance with the commitments made by the Respondent; notably its commitment to pay the monies due to the Banks as manifested by the Payment Agreement, the Mortgage Contract, the [REDACTED] Letter and the oral commitments made by several representatives of the Respondent to the Banks;
  - (3) The annulment of the Payment Agreement and the Mortgage Contract, followed by the deletion of the mortgages from the Estonian Ship Register; and
  - (4) Unjust actions by the Respondent towards the Banks in relation to the bankruptcy of RAS Ookean.
211. The Banks contended that the Respondent's conduct amounted to violations of the protection provided by the two BITS, notably the requirements of fair and equitable treatment and full security and protection; the provisions forbidding nationalisation or expropriation without due compensation; and the provision requiring that commitments made are honoured. As the Claimants, of course, the Banks bear the burden of establishing their respective cases against the Respondent.

***(B) Fair and Equitable Treatment: Relevant Legal Principles***

212. The primary ground on which the Banks have alleged a breach of both applicable BITs is, as noted above, the “fair and equitable treatment” provision. It is necessary first to establish the relevant scope of these legal standards under the two BITs, before applying these standards to the facts of this case as found by the Tribunal.

213. Article 3 of the Estonia-Finland BIT provides, in the English version:

*“Each Contracting Party shall, subject to its laws and regulations and in conformity with international law, at all times ensure a fair and equitable treatment to the investments of investors of the other Contracting Party”.*

(The English version was agreed to prevail by the Contracting States, in case of any dispute over the Finnish and Estonian versions).

214. Article 2(1) of the Estonia-Germany BIT provides, as translated from the German text:

*“Each Contracting Party shall in its territory and in accordance with its legal provisions permit and if possible promote investments of citizens or companies of the other Contracting Party. Such investments must in all events be treated in a just and equitable manner.”*

(The final sentence in the original German version reads: *“Sie wird Kapitalanlagen in jedem fall gerecht und billig behandeln”*. The German and Estonian versions are equally binding upon the Respondent; and the English translation of both supplied to the Tribunal was not disputed between the Parties).

215. Accordingly, the first question is the legal meaning in the BITs of these two apparently different phrases, as quoted above: “fair and equitable treatment” and (as translated) “just and equitable manner”. The Tribunal can see no substantive difference between standards requiring a fair and equitable treatment and a just and equitable manner; and for convenience, both are here described collectively as the “FET standard”.

216. However, as already noted above, the FET standard in Article 3 of the Estonia-Finland BIT is expressly qualified: “in conformity with international law”. This same qualification is missing from Article 2(1) of the Estonia-Germany BIT. The next question, therefore, is whether this linguistic difference produces a juridical difference as a matter of treaty interpretation. The difference is relevant to this case because it could suggest, by the express reference to international law, that the FET standard in the Estonia-Finland BIT is not an “autonomous” standard but reflects only the lesser minimum standard of protection for investors established by customary international law
217. ***Autonomous Standard:*** It is appropriate to consider first the meaning of the FET standard, without this express reference to international law, as expressed in the Estonia-Germany BIT.
218. Dr F.A. Mann QC, in his 1981 commentary on the FET standard in the model United Kingdom BIT/IPPA<sup>20</sup>, expressed the view:

*“[...] that nothing is gained by introducing the conception of a minimum standard and, more than this, it is positively misleading to introduce it. The terms „fair and equitable treatment“ envisage conduct which goes far beyond the minimum standard and afford protection to a greater extent and according to a much more objective standard than any previously employed form of words. A tribunal would not be concerned with a minimum, maximum or average standard. It will have to decide whether in all circumstances the conduct in issue is fair and equitable or unfair and inequitable. No standard defined by other words is likely to be material. The terms are to be understood and applied independently and autonomously.”*

219. Dr Mann also wrote, in 1982, in the fourth edition of *Legal Aspect of Money*<sup>21</sup>:

*“[...] In some cases, it is true, treaties merely repeat, perhaps in slightly different language, what in essence is a duty imposed by customary international law; the foremost example is the familiar provision whereby States undertake to „accord fair and equitable treatment“ to each other“s nationals, and to which in law is unlikely to amount to more than a confirmation of the obligation to act in good faith, or to refrain from abuse or arbitrariness.”*

---

<sup>20</sup> F. A. Mann, “British Treaties for the Promotion and Protection of Investments”, (1981) 52 *BYIL* 241, p. 244.

<sup>21</sup> F. A. Mann, *The Legal Aspect of Money* (4<sup>th</sup> ed, 1982), p. 510 (footnote omitted).

The apparent contrast is instructive: it demonstrates at least the elusive nature of the FET standard and, at the time, the difficulties in defining its legal content and application beyond its obvious and immediate characteristics.

220. Professor Vandeveldel, in his 1992 work on the USA's investment treaty practice<sup>22</sup>, advanced the view that an express FET standard in a BIT was intended to add protection for the investor greater than that provided by the minimum standard of treatment provided by customary international law:

*“The clause [in the USA's model BITs of 1983-1987 providing for “fair and equitable treatment”] provides a baseline of protection which will be useful principally in situations where other substantive provisions of international and national law provide no protection.”*

221. Professor Rudolf Dolzer and Ms Margrete Stevens, in their 1995 work on BITs, expressed a similar view<sup>23</sup>:

*“[...] the fact that the parties to BITs have considered it necessary to stipulate this standard as an express obligation rather than relied on a reference to international law and thereby invoked a relatively vague concept such as the minimum standard, is probably evidence of a self-contained standard.”*

Significantly, for present purposes, these authors add:

*“Further, some treaties refer to international law in addition to the fair and equitable treatment, thus appearing to reaffirm that international law standards are consistent with, but complementary to the provisions of the BIT”.*

222. The 1999 UNCTAD research paper on Fair and Equitable Treatment stated<sup>24</sup>:

*“If States and investors believe that the fair and equitable standard is entirely interchangeable with the international minimum standard, they could indicate this clearly in their investment instruments; but most investment instruments do not make an explicit link between the two standards. Therefore, it cannot be readily argued that most States and investors believe fair and equitable treatment is implicitly the same as the international minimum standard.”* Its conclusion, based on state practice, was as follows: *“These considerations point ultimately towards fair and equitable treatment not being synonymous with the international*

---

<sup>22</sup> Kenneth J. Vandeveldel, *United States Investment Treaties: Policy and Practice*, (Cambridge: Kluwer Law International, 1992), p. 76.

<sup>23</sup> Rudolf Dolzer and Margrete Stevens, *Bilateral Investment Treaties*, (Kluwer Academic Publishers Group, 1995), p. 60.

<sup>24</sup> “Fair and equitable treatment”, *UNCTAD series on issues in international investment agreements*, (1999). pp 13 and 40 (The 2004 UNCTAD Research Paper on “Fair and Equitable Treatment Standards in International Law re-stated this approach, at p. 24).

*minimum standard. Both standards may overlap significantly with respect to issues such as arbitrary treatment, discrimination and unreasonableness, but the presence of a provision assuring fair and equitable treatment in an investment instrument does not automatically incorporate the international minimum standard for foreign investors. Where the fair and equitable standard is invoked, the central issue remains simply whether the actions in question are in all the circumstances fair and equitable or unfair and inequitable.”*

223. In another review of state practice in 2000, Dr Vasciannie also concluded that the FET standard expressed in a BIT without more, was autonomous<sup>25</sup>:

*“[...] it is noteworthy that the instances in which States have indicated or implied an equivalence between this standard and the international minimum standard are relatively sparse. Moreover, bearing in mind that the international minimum standard has itself been an issue of controversy between developed and developing States for a considerable period, it is unlikely that a majority of States would have accepted the idea that this standard is fully reflected in the fair and equitable standard without clear discussion. These considerations point ultimately towards the conclusion that the two standards in question are not identical: both standards may overlap significantly with respect to issues such as arbitrary treatment, discrimination and unreasonableness, but the presence of a provision assuring fair and equitable treatment in an investment instrument does not automatically incorporate the international minimum standard for foreign investors. Following Mann [i.e. the 1981 work cited above], where the fair and equitable standard is invoked, the central issue remains simply whether the actions in question are in all the circumstances fair and equitable or unfair and inequitable.”*

224. Professor Muchlinski reached a similar conclusion in 2004<sup>26</sup>:

*“It has been suggested that fair and equitable treatment represents a classical international law standard which embodies international minimum standards of treatment. [...]. If the intention is to assimilate the two concepts, this should be made explicit in the text. Otherwise, the fair and equitable treatment standard should stand on its own.”*

225. This scholarly analysis, based on decades of multi-state practice, is also confirmed by decisions of arbitration tribunals, particularly the recent awards of the tribunals in *Saluka v. Czech Republic* (2006), *Azurix v. Argentina* (2006) and *Occidental v. Ecuador* (2004)<sup>27</sup>.

---

<sup>25</sup> Stephen Vasciannie, “Fair and Equitable Treatment” (2000) 70 *BYIL* 99.

<sup>26</sup> Peter T. Muchlinski, *Multinational Enterprises and The Law*, (2004), pp. 625-626.

<sup>27</sup> *Saluka Investments BV v The Czech Republic*, Partial Award of 17 March 2006, available at <http://ita.law.uvic.ca>; *Azurix Corp. v. Argentine Republic* (ICSID Case No. ARB/01/12), Award of 14 July 2006, available at

226. In *Saluka*<sup>28</sup>, the tribunal declined the invitation to assimilate that particular BIT's express FET standard with the minimum standard under customary international law:

*"Whichever the difference between the customary and the treaty standards may be, this Tribunal has to limit itself to the interpretation of the "fair and equitable treatment" standard as embodied in Article 3.1 of the Treaty. That Article omits any express reference to the customary minimum standard. The interpretation of Article 3.1 does not therefore share the difficulties that may arise under treaties (such as the NAFTA) which expressly tie the "fair and equitable treatment" standard to the customary minimum standard. Avoidance of these difficulties may even be regarded as the very purpose of the lack of a reference to an international standard in the Treaty. This clearly points to the autonomous character of a "fair and equitable treatment" standard such as the one laid down in Article 3.1 of the Treaty."*

227. In *Azurix*<sup>29</sup>, the tribunal was required to interpret an FET standard in a BIT which also provided, in a third sentence, that investors should in no case "be accorded treatment less than that required by international law." This tribunal concluded:

*"The clause, as drafted, permits to interpret fair and equitable treatment and full protection and security as higher standards than required by international law. The purpose of the third sentence is to set a floor, not a ceiling, in order to avoid a possible interpretation of these standards".*

The tribunal there clearly distinguished between the autonomous standard of an express provision in a treaty and the minimum standard imposed by customary international law.

228. In *Occidental*<sup>30</sup>, the tribunal declined on the facts of that case required for its decision, to determine whether the FET standard in the USA-Ecuador BIT was the same as the minimum standard under customary international law:

---

<http://www.worldbank.org/icsid>; *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467 Award of 1 July 2004, available at <http://ita.law.uvic.ca>. These awards were not cited to the Tribunal in these proceedings; but it is nonetheless useful to refer to these and like materials as confirming the approach upon which the Tribunal has already decided based on materials and arguments submitted by the Parties.

<sup>28</sup> *Saluka Investments BV v The Czech Republic*, Partial Award of 17 March 2006, para 294, available at <http://ita.law.uvic.ca>.

<sup>29</sup> *Azurix Corp. v. Argentine Republic* (ICSID Case No. ARB/01/12), Award of 14 July 2006, available at <http://www.worldbank.org/icsid>, para. 361.

<sup>30</sup> *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467, Award of 1 July 2004, available at <http://ita.law.uvic.ca>, para. 192.

*“The question whether there could be a Treaty standard more demanding than a customary international law standard that has been painfully discussed in the context of NAFTA and other free trade agreements does not therefore arise in this case. The case here is rather to ensure both the stability and predictability of the governing legal framework”.*

(The tribunal decided that an alteration of the legal and business environment, in which the investment had been made, could “trigger treatment that is not fair and equitable”).

229. It would be possible to continue these citations of awards to similar effect; and there are several with passages which may be understood as qualifying the outer boundaries of the approach taken above; but none have affected the decision of the Tribunal in this case. For obvious reasons, the Tribunal has considered the ICSID award in *Genin v. Estonia* (2001), decided under the Estonia-USA BIT of 1994 (entering into force on 16 February 1997)<sup>31</sup>. Article II, Paragraph 3(a) of this BIT provides for the “fair and equitable” treatment of investments and requires that no investment shall be accorded treatment less favourable than that required by international law. The tribunal decided that the respondent had not violated this provision, applying “the international minimum standard”, including “acts showing a wilful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith” (paragraph 367, pp. 299-300). Given its different wording, that the tribunal considered that “the exact content of this standard is not clear” and also defined its content with such non-exhaustive examples, this Tribunal considers that its decision in this Award is consistent with the *Genin* award.
230. In conclusion, having regard specifically to the Estonia-Germany BIT’s object and purpose and in particular the wording of Article 2(1) and generally to these international legal materials, the Tribunal considers that the FET standard in the Estonia-Germany BIT bears an autonomous meaning and that it is not to be assimilated to the lesser minimum standard of treatment under customary international law.

---

<sup>31</sup> *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. The Republic of Estonia*, (ICSID Case No. ARB/99/2), Award of 25 June, 2001, available at <http://www.worldbank.org/icsid>.

231. ***“International Law”***: With regard to the Estonia-Finland BIT, it is the Tribunal’s view that, without the express reference to international law, Article 3 of the Estonia-Finland BIT would bear the like autonomous meaning to Article 2(1) of the Estonia-Germany BIT. The next question, therefore, is whether that reference lowers this BIT’s FET autonomous standard to the minimum standard under customary international law.

232. A similar issue, as is well-known, arose over the interpretation of Article 1105(1) of NAFTA. Its FET standard provides:

*“Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.”*

233. In several investor-state arbitrations under NAFTA’s Chapter XI, it was debated whether this FET standard provided only the minimum standard of treatment under customary international law or a greater autonomous standard.

234. This debate was famously curtailed, initially at least, when Article 1105(1) NAFTA was interpreted by the NAFTA Free Trade Commission (“FTC”) on 31 July 2001 (in relevant part) as follows:

*“(1) Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party. (2) The concepts of “fair and equitable treatment” and “full protection and security” do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.”*

235. The FTC’s interpretation is, of course, to be accorded appropriate weight; but it is not legally binding on this Tribunal; and even if it were, it cannot be conclusive on the particular question facing this Tribunal. In the Tribunal’s view, the wording of Article 3 of the Estonia-Finland BIT is materially different from Article 1105(1) NAFTA: the term “in conformity with” is not the same as the term “in accordance with”. Article 3 does not therefore prescribe treatment in accordance with international law with an FET standard as a subsidiary rule of customary international law, as was noted by the *Saluka* tribunal (cited



- above). To the contrary, as indicated by Dolzer & Stevens, the reference to international law reaffirms “that international law standards are consistent with, but complimentary to the provisions of the BIT” (cited above); and it is not therefore intended as a “ceiling”.
236. Accordingly, the Tribunal considers that the FET standard in Article 3 of the Estonia-Finland BIT bears an autonomous meaning, and like the Germany-Finland BIT, is not to be assimilated to the lesser minimum standard treatment under customary international law. However, there is a potential difference between these BIT’s two autonomous meanings. As regards the Estonia-Finland BIT (unlike the Estonia-Germany BIT), the Tribunal must still give effect to its reference to international law, which is expressed as a form of qualification to its FET standard. This reference cannot here be disregarded by the Tribunal as meaningless or redundant as a matter of treaty interpretation.
237. In the Tribunal’s view, these Contracting Parties intended, by this reference, to ensure that their BIT’s FET standard was not to be interpreted as a wholly autonomous concept, thereby enabling a tribunal (arguably) to apply its own subjective or impressionistic conclusions as to whether a respondent state had acted “fairly” or “equitably”, but rather to ensure that their FET standard was a recognized and defined standard in international law. The next question, therefore, is what is this recognized and defined standard, given that it is not the minimum standard under customary international law?
238. Such an FET standard is difficult to define, in the abstract, as a matter of international law. The term remains significantly ambiguous and imprecise; it cannot be determined by reference to a dictionary; and it is clearly not synonymous with “equity” under national laws, or even common notions of “fairness” (which may differ between investors and capital-importing states and between states with developing and developed economies). Whilst, in the Tribunal’s view, its meaning significantly overlaps with the minimum standard under customary international law, this FET standard clearly provides a greater protection for the foreign investor. According to the minimum standard under customary international law, an investor is protected against the host state’s fraud,

bad faith, capricious and wilful discrimination or where the host state “deprives an investor of acquired rights in a manner that leads to the unjust enrichment of the State”<sup>32</sup>. The FET standard in the Estonia-Finland BIT must therefore give greater protection than this; but it is plain that it is easier to apply this FET standard case than to define it. As the tribunal noted in the *Mondev* case:

*“A judgment of what is fair and equitable cannot be reached in the abstract; it must depend on the facts of the particular case”*.<sup>33</sup>

239. It is therefore helpful to consider what arbitration tribunals have decided in practice, in specific cases, particularly in *Neer* (1928), *Waste Management* (2003), *Tecmed* (2003) and *Thunderbird* (2006) and, most recently the decision of the ICSID *Ad Hoc* Committee in *MTD Equity v. Chile* (2007).

240. In *The Neer Case*<sup>34</sup>, which did not concern an investment dispute, the tribunal applied an FET standard under customary international law, requiring its breach to amount:

*“to an outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognise its insufficiency”*.

It follows that the FET standard in the Estonia-Finland BIT, providing a greater protection for the investor than customary international law, can be broken by the host state with treatment falling short of such egregious “outrage, bad faith etc”. In other words, malign intent, bad faith or malice are not required for a breach of this FET standard.

241. In *Waste Management*<sup>35</sup>, the tribunal noted by reference to decisions in past NAFTA cases over its FET standard:

*“[...] the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the*

---

<sup>32</sup> UNCTAD, *Fair and Equitable Treatment*, (1999), p. 12.

<sup>33</sup> *Mondev International Ltd. v. United States of America* (ICSID Case No. ARB(AF)/99/2), Award of 11 October 2002 available at <http://www.state.gov/documents/organization/14442.pdf>, para. 118.

<sup>34</sup> *Neer v. Mexico*, 4 RIAA 60 (Gen. Cl. Comm’n 1926); 3 AD 213..

<sup>35</sup> *Waste Management, Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3), Award of 30 April 2004, available at <http://ita.law.uvic.ca>, para. 98.

*conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.”*

The Tribunal here notes, in particular, the reference to conduct of the host state that is “arbitrary, grossly unfair, unjust or idiosyncratic” and the reference to treatment in breach of representations made by the host state.

242. In *Tecmed v Mexico*<sup>36</sup>, the tribunal decided in its award:

*“[154] The Arbitral Tribunal considers that this provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. ... The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any pre-existing decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities.”*

The Tribunal here notes, in particular the reference to the investor’s “basic expectations”.

243. Again, however, the FET standard in the Estonia-Finland BIT grants still greater protection than the minimum standard; but in the light of the recent decision in *MTD Equity v. Chile*, it may be necessary to qualify this tribunal’s particular approach to the investor’s “basic expectations” (as noted further below).

---

<sup>36</sup> *Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, (ICSID Case No. ARB (AF)/00/2), Award of 29 May 2003, available at <http://ita.law.uvic.ca>, para 154; applied in *MTD Equity Sdn. Bhd. & MTD Chile S.A. v Chile*, (ICSID Case No. ARB/01/7), Award of 25 May 2004, available at <http://ita.law.uvic.ca>; *CMS Gas Transmission Company v. Argentine Republic*, (ICSID Case No. ARB/01/8), Decision of the Tribunal on Objections to Jurisdiction of 17 July 2003, available at <http://www.worldbank.org/icsid>; and *Eureko BV v. Republic of Poland*, Partial Award of 19 August 2005, available at <http://ita.law.uvic.ca>.

244. In *Thunderbird v. United Mexican States*<sup>37</sup>, the tribunal similarly suggested that, in order to establish a case based on the investor's expectations, it was necessary that there be conduct on the part of the State creating "reasonable and justifiable expectations on the part of an investor (or investment) to act in reliance on said conduct". Having regard to the recent decision in *MTD Equity v. Chile*, it may be necessary also to qualify this tribunal's particular approach to the investor's "expectations".
245. In *MTD Equity v. Chile*<sup>38</sup>, the ICSID *Ad Hoc* Committee was invited to criticise "the Tecmed programme for good governance" and to decide that the *Tecmed dictum* (in paragraph 154 of the award, cited above) did not reflect international law. The Committee clearly accepted certain of these criticisms:

*"For example, the TECMED Tribunal's apparent reliance on the foreign investor's expectations as the source of the host State's obligations (such as the obligation to compensate for expropriation) is questionable. The obligations of the host State towards foreign investors derive from the terms of the applicable investment treaty and not from any set of expectations investors may have or claim to have. A tribunal which sought to generate from such expectations a set of rights different from those contained in or enforceable under the BIT might well exceed its powers, and if the difference were material might do so manifestly."*

The Committee did not however exclude the relevance of "legitimate expectations". It approved as "defensible" the tribunal's formulation in the challenged award: *"In terms of the BIT, fair and equitable treatment should be understood to be treatment in an even-handed and just manner, conducive to fostering the promotion of foreign investment. Its terms are framed as a proactive statement - „to promote“, „to create,“ „to stimulate“ - rather than prescriptions for a passive behavior of the State or avoidance of prejudicial conduct to the investors."* The Committee also recognised that the extent to which a State is obliged under the FET standard to be pro-active is open to debate, *"but that is more a question of application of the standard than it is of formulation."* The Tribunal notes this significant distinction.

---

<sup>37</sup> *International Thunderbird Gaming Corporation v. United Mexican States*, Award of 26 January 2006, para. 14 et seq., available at <http://ita.law.uvic.ca>.

<sup>38</sup> *MTD Equity Sdn. Bhd. & MTD Chile S.A. v. Chile*, (ICSID Case No. ARB/01/7), Ad Hoc Committee Decision on the Application for Annulment of 21 March, 2007, available at <http://ita.law.uvic.ca>, para. 70 and 71

246. In this case, for two reasons, it is unnecessary for this Tribunal to resolve the debate over the exact content of the minimum standard under international law, which will doubtless continue for many years. First, the issue here, as decided above by the Tribunal, relates to an autonomous FET standard providing greater protection to a covered investor than the minimum standard. Second, as decided below by the Tribunal, that FET standard is here applicable to a specific representation made by the host state to the investor (the ██████ Letter) in the context of an existing dispute and not a general pre-existing “set of expectations” claimed by an investor because these “were taken into account by the foreign investor to make the investment”.
247. In conclusion, having taken into account generally the object and purpose of the Estonia-Finland BIT and, in particular, the wording of Article 3, the Tribunal considers that a breach of its FET standard can be established by reference (*inter alia*) to an investor’s expectations of even-handed and just treatment by the host state induced by that state’s unequivocal representation directed at that investor, provided that these expectations are reasonable and justifiable. It follows that, where such a representation is made by the host state under this BIT, the factual issue is whether in all the circumstances it was reasonable and justifiable for the investor to rely upon that representation; and, if so, whether there was in fact such reliance. This follows not merely as part of the FET standard as regards breach of the BIT, but also because the Tribunal is required to identify, as regards any decision on compensation, the actual loss suffered by the investor as a result of the host state’s breach of this FET standard. In a case where there is no reliance, the investor may have suffered no loss when the host state acts inconsistently with its representation. By contrast, where on the basis of an unequivocal representation made by the state, the investor makes or maintains its investment, or otherwise acts to its detriment, there may be a loss to the investor where the state acts inconsistently.
248. Thus, in the present case, it will be necessary for the Tribunal to identify under Article 3 of the Estonia-Finland BIT, in particular, (i) whether there was any such unequivocal representation made by or on behalf of the Respondent to the Banks;

- (ii) whether the Banks relied on that representation, such reliance being reasonable and justifiable in all the circumstances; (iii) whether the Respondent acted inconsistently with its representation; and (iv) what actual loss, if any, resulted from the Respondent's failure to act consistently with its representation.
249. In arriving at this conclusion under Article 3 of the Estonia-Finland BIT, the Tribunal acknowledges that it may be applying a different FET standard than the standard required under Article 2(1) of the Estonia-Germany BIT. However, given that the latter creates no lesser protection to the investor than the former, a decision that the Respondent has not complied with the FET standard in the Estonia-Finland BIT would inevitably mean that a breach had been established under the Estonia-Germany BIT.

***(C) Fair and Equitable Treatment: Relevant Facts***

250. With regard to the Banks' first factual complaint, the exhaustion of Estrôbprom's assets, it is clear that, by letter dated 29 November 1988,<sup>39</sup> the Director-General of Estrôbprom confirmed that the assets of Estrôbprom included, amongst others, an ocean fleet consisting of 57 vessels, a fishing factory in Pärnu, a fishing harbour in Tallinn, a shipyard, a fishing equipment factory and a cold storage. It is probable that the Banks, as they submit, based their decision to grant the Loan to a material extent on this information. The Banks were, of course, consciously taking a huge political risk in advancing substantial monies to a Soviet borrower in Estonia: the status of Estonia, occupied by the USSR since 1940, remained highly controversial politically and legally; and even within the USSR at that time, it was not regarded as impossible that Estonia might both regain a significant measure of autonomy, if not eventual independence from the USSR.
251. After the Respondent became independent from the USSR in August 1991, the Supreme Council of Estonia declared the property or assets of any companies, associations or organisations in the territory of Estonia operating under the control

---

<sup>39</sup> Exhibit C3.

- or subordination of any Soviet administration as the property of the Respondent. On 12 September 1991, the Estonian Government passed the Decree No. 182 on the implementation of the Supreme Council's decision. As an attachment to the Decree was a list of the companies which (with their assets) were declared to be property of the Respondent. Amongst these listed companies was Estrõbprom<sup>40</sup>.
252. The Tribunal considers RAS Ookean as the eventual legal successor to Estrõbprom and that RAS Ookean received in such capacity Estrõbprom's remaining assets. As recited in the chronology in Part II of this Award, Estrõbprom was succeeded by Eesti Kalatõõstus and the latter acquired Estrõbprom's assets; RE Ookean was the legal successor to Eesti Kalatõõstus and acquired its assets; and RAS Ookean in turn succeeded to RE Ookean and acquired its assets.
253. The question whether, at some point in time at or after the Respondent's independence, the Respondent also acquired legal ownership of any of these assets, is not relevant to the Tribunal's decisions in this Award, whether in the form of "state-ownership" previously enjoyed under Soviet law by the USSR or otherwise. The Tribunal is satisfied that, at the date of incorporation of RAS Ookean in July 1993, assets were transferred to it from RE Ookean<sup>41</sup>. Moreover, by September 1993 (as evidenced by the ██████████ Letter), the Respondent treated the vessels described in the Payment Agreement as the property of RAS Ookean. Still further, RAS Ookean paid old Estrõbprom bills<sup>42</sup>; RAS Ookean was treated as responsible for the Estrõbprom Guarantee as its legal successor<sup>43</sup>; and there was no material distinction made between RAS Ookean's assets and Estrõbprom's assets<sup>44</sup>. Indeed, both RE and RAS Ookean were generally considered at the time to be the successors of Estrõbprom<sup>45</sup>.
254. As already noted above, attached to its Articles of Association upon the incorporation of RAS Ookean, was a list of its assets. These assets included fifty

---

<sup>40</sup> The Banks' submission was not materially disputed by the Respondent: see its Counter Memorial, para. 35.

<sup>41</sup> See the Attachment to RAS Ookean's Articles of Association, Exhibit. 2.

<sup>42</sup> Mr ██████████ Testimony, Transcript pp. 381-82; Mr ██████████ Testimony, Transcript p. 1071; Mr ██████████ Testimony, Transcript p. 1341.

<sup>43</sup> Mr ██████████ Testimony, Transcript pp. 506 and 531.

<sup>44</sup> Mr ██████████ Testimony, Transcript, p. 700.

<sup>45</sup> Mr ██████████ Testimony, Transcript pp. 1071 and 1133; Mr ██████████ Testimony, Transcript p. 1186.

vessels, a shipyard, a refrigeration plant, a hotel, a car depot, navigation unit etc. The assets book value mentioned was EEK 462,471,000.00<sup>46</sup>.

255. At least the following substantial assets were transferred out of the company after 1993 by the Respondent:<sup>47</sup> the Pärnu Fish Processing Factory; the Tallinn Sailors Hospital and Outpatient Department; the Kopli Port; the cold storage; and the fleet of fishing vessels.
256. The Tribunal does not consider that the participation of the Estonian Government in these activities constituted any breach of the FET standard. It must be recalled, in particular, that the events in the USSR leading up to August 1991 were turbulent in the extreme; and that after the Respondent's independence from the USSR, the dissolution of the USSR was and remained politically, legally and economically chaotic. The Respondent had to surmount enormous difficulties; and these difficulties continued long after 1991, including the period from December 1992 onwards upon which the Banks here rely.
257. The next breach asserted by the Banks is non-compliance by the Respondent with its "commitments", with particular weight being given to the Payment Agreement and the [REDACTED] Letter.
258. In the Payment Agreement, Recital (D) reads as follows:
- "At the meetings held in Tallinn on June 4th and 7th 1993 representatives of the Ministry of Economy and Ookean stated that they intend to repay the ESVA loan despite current legal disputes and they are prepared to enter into a commitment to the Banks to that effect and to sell certain assets for the specific purpose of paying off the ESVA loan."*
259. RAS Ookean then committed itself towards the Banks in accordance with the Payment Agreement's terms, already described above in Part II of this Award. In summary, RAS Ookean's commitment was to mortgage and sell the six vessels in order to pay the balance of the Loan to the Banks. This is manifestly clear from

---

<sup>46</sup> See Exhibit C24.

<sup>47</sup> These facts were not materially disputed by the Respondent: see its Counter-Memorial para. 63.; and see also Mr [REDACTED] Testimony, Transcript, pp. 392-93, 469 and 514 and Mr [REDACTED] Testimony, Transcript p. 1313.



the Payment Agreement itself, and also from witness testimony adduced in these arbitration proceedings<sup>48</sup>.

260. The [REDACTED] Letter clearly related to the Payment Agreement. The Payment Agreement provided that this letter, which was in draft form attached to the agreement as a Schedule, would be delivered by the Estonian Government. As already described above, it was so delivered by the Respondent, signed by its Minister, Mr [REDACTED]

261. The relevant part of the [REDACTED] Letter (*inter alia*) provided:

*"[2] Ookean Ltd shall ... use all funds from the sale of these vessels for the purpose of repaying the ESVA Loan in accordance with the above agreement [i.e. the Payment Agreement].*

*[3] The Board of Ookean shall through their capacity and the authority invested in them by the Ministry, exercise their rights and powers in such a manner as to ensure that Ookean Ltd complies with the obligations stipulated in this agreement."*

(The Tribunal does not consider that the Banks' case is advanced by subparagraph 1 of the [REDACTED] Letter).

262. It is important to state first what, in the Tribunal's view, the legal significance which this letter did *not* bear: it was not a guarantee; nor an indemnity; nor a "near-guarantee"; nor indeed of any contractual significance under the national law or laws applicable to the Payment Agreement (accordingly, the [REDACTED] Letter could not found any claim for breach of Articles 4 of the Estonia-Finland BIT and 8(2) of the Estonia-Germany BIT concerning observance of obligations/commitments with regard to investments).

263. Nonetheless, in the opinion of the Tribunal having regard to all the circumstances in which the letter was made at that time, these terms constituted an unequivocal representation by the Respondent to the Banks by which the Banks could reasonably and justifiably expect, as they did, that the balance of the Loan, as it

---

<sup>48</sup> E.g. Mr [REDACTED] Testimony, Transcript p. 551.

stood on 17 September 1993, would eventually be repaid by RAS Ookean at the direction of the Board and, in turn, the Respondent.

264. In coming to this conclusion, the Tribunal has taken fully into account that the ██████ Letter did not come suddenly out of the blue. It was the natural culmination of protracted negotiations with the Respondent on the financial problems of ESVA and Ookean and of their incapacity to repay the Loan to the Banks over a long period. The Estonian Government had long expressed concern about this default to the Banks; and it had sought, overtly, different ways and means to have the Loan repaid to the Banks. For example, in June 1992, as appears from minutes of the Board meeting of RAS Ookean held at the Estonian Ministry of Industry of 1 July 1992, the impression was created by Mr ██████ ██████ the Deputy Minister, that the Ministry, as the effective owner of RAS Ookean, would ensure that the Banks would not suffer any loss or rights if they should refrain from formal legal action against Ookean or ESVA.

265. As regards this meeting, Mr ██████ testified as follows:

*“Mr ██████ let us know that possibly a guarantee by the Estonia government could be given or a new guarantee by Ookean with the signatures of the concerned ministries, which in his opinion would be almost equal to that of the government.”<sup>49</sup>*

And the minutes of that meeting report:

*“Deputy Minister ██████ stated that the Ministry of Industry [...], as representative of the owner of Ookean will ensure that the Banks will not suffer any loss of rights if they shall refrain from formal legal action against Ookean or ESVA.”<sup>50</sup>*

266. It is significant that, when the Respondent's Ministry of Economy appealed against ESVA's bankruptcy, the Ministry stated in that appeal:

---

<sup>49</sup> Exhibit C9; see also Mr ██████ Testimony, Transcript pp. 597-8, 602, 611; Mr ██████ Testimony, Transcript p. 733; Mr ██████ Testimony, Transcript pp. 1222, 1241.

<sup>50</sup> Exhibit C9; see also Mr ██████ Testimony, Transcript pp. 743-4.

*“[...] a third party, RAS Ookean, presented a composition proposal during the hearing, agreeing to sell six vessels type "Moonsund" to cover the debts. The Ministry of Economic Affairs has accepted the matter in question.”*<sup>51</sup>

This “acceptance” by the Ministry for RAS Ookean speaks for itself.

267. It is also significant that generally in these negotiations with the Banks, not only Ookean took part but also senior officers of the Estonian Government. All the Estonian officers mentioned by the witnesses during the Hearing, Mr ██████ Mr ██████ and Mr ██████ held high ranking positions in their respective Ministries. When Mr ██████ was asked whether it was possible that officers from his Ministry could negotiate with the Banks without his knowledge, he answered firmly in the negative.<sup>52</sup> This included, of course, the negotiations for the Payment Agreement<sup>53</sup>.
268. Moreover, the practical borderline between RAS Ookean and the Estonian Government, notably the Ministry of the Economy, was rather thin. The Tribunal is satisfied that, apart from its formal status under public law, the Government had a firm grip on RAS Ookean and the management of its affairs. Both the Ministry of Economy and the Ministry of Finance had representation on its Board; and those representatives even formed the majority of the Board.<sup>54</sup> From a formal point of view, those representatives were doubtless under an obligation, when exercising their duties as Board members, to act independently of the Government and in the interest of the company and, possibly, its creditors. But practice is sometimes more complex; and the Tribunal considers it probable that, especially in the transition period following independence from the USSR, form and substance were different. The Tribunal is therefore not surprised that Mr ██████ and others testified that the real decisions for RAS Ookean were taken at government level. That “[...] the Ministry ran the company through a board

---

<sup>51</sup> Exhibit C20.

<sup>52</sup> Mr ██████ Transcript p. 865.

<sup>53</sup> Of which Mr ██████ said that he did not know the contents ██████ Transcript p. 872.

<sup>54</sup> See Mr ██████ Testimony, Transcript p. 1067.

- [...]”<sup>55</sup> may not be correct from a formal point of view; but it is probable that this is generally what happened in practice<sup>56</sup>.
269. It would be possible to add to these evidential references extensively. It is unnecessary to do so here. All the evidence, in the Tribunal’s view, was overwhelming and one-sided in its overall effect.
270. At the time of the Payment Agreement, the Banks clearly relied on the ██████ Letter. The negotiations leading to the Payment Agreement were triggered by the bankruptcy proceedings of Ookean and ESVA; and the bankruptcy of Ookean and other legal actions were terminated on the basis of the Payment Agreement both in Estonia and Finland. If the Payment Agreement had not been concluded, the Banks would have pursued their legal actions for the immediate repayment of the outstanding Loan; and without the ██████ Letter, the Banks would not have made the Payment Agreement. The Payment Agreement was a major concession by the Banks. Again, in the Tribunal’s view, the evidence for these conclusions is overwhelming.
271. The fact that, much later, the Payment Agreement was declared invalid under Estonian law by the Supreme Court of Estonia in November 2001 does not mean that the ██████ Letter lost its significance under the BITs as a matter of international law. It never had, as the Tribunal has decided above, any contractual significance or legal effect under any national law.
272. The Tribunal has taken into account that Mr ██████ in his oral testimony, denied that either he or his Ministry ever intended to make any promise or representation that the Banks would get paid under the Estrôbprom Guarantee.<sup>57</sup> The Tribunal accepts that no contractual promise was ever made by the Respondent; but it cannot give any further weight to this testimony, as compared to the terms of the ██████ Letter and its contemporary events. The Respondent

---

<sup>55</sup> Mr ██████ Testimony, Transcript p. 380, 502. Mr ██████ Testimony, Transcript pp. 1067, 1095, 1101, and 1161.

<sup>56</sup> See also Mr ██████ Testimony, Transcript p. 1398 on his strong reluctance to sign the Payment Agreement: “[...] as a person I was against signing the Agreement, but is also a fact that me [sic]), as a director of a State enterprise, did not want to contradict the Board in this serious issue and I did not want to confront the Ministry.”

<sup>57</sup> E.g. Mr ██████ Testimony, Transcript p. 783.

was manifestly trying to find some means to get the Loan repaid to the Banks; so were the Banks; this was the general spirit of the Estonian Government's attitude towards the Banks at that time<sup>58</sup>; and the [REDACTED] Letter was the natural and concrete result.

273. The Tribunal has also taken into account Mr [REDACTED]'s interpretation of his letter, but the Tribunal has some difficulty in following that interpretation. For example, the Tribunal cannot accept that Paragraph [3] of the [REDACTED] Letter is nothing more than a "courtesy sentence"<sup>59</sup>. It is far more than that, as already decided above. In this context, the Tribunal also notes that Mr [REDACTED] accepted that his letter should not be considered on a stand-alone basis but together with the Payment Agreement<sup>60</sup>. It cannot therefore be a mere "courtesy" letter, still less "unofficial", as was submitted by the Respondent in these proceedings.

274. The Respondent also submitted that the [REDACTED] Letter was illegal, even patently illegal under Article 65 of the Respondent's Constitution. This submission is not accepted by the Tribunal. Under the applicable BITs, it is the obligation of the host State to deal with covered investments in accordance with the FET standard. If legitimate expectations are raised by the Respondent with a specific foreign investor that his investment will be treated fairly and equitably, such expectations must be honoured as a matter of international law. The fact that, according to the law of the host country, its officials or minister(s) may need certain internal approvals cannot later be held against that investor so as to defeat those expectations. Moreover, the Tribunal does not consider that the [REDACTED] Letter was made illegally under the laws of Estonia, or otherwise: it was not a legal binding financial commitment under Estonian law.

---

<sup>58</sup> Mr [REDACTED] Testimony, Transcript p. 1406: "[...] the Ministry wished to support Ookean and to improve its economic situation" and p. 1460: "When it was RAS or RE, all the boards existed for a relatively short time, and in such a situation they did not have any specific concrete tasks given by the State or by the Ministry, except for that one important problem that the Finnish banks raised."

<sup>59</sup> Mr [REDACTED] Testimony, Transcript p. 881.

<sup>60</sup> Mr [REDACTED] Testimony, Transcript pp. 895-96.

*(D) The Tribunal's Decision*

275. The question is whether the Respondent honoured its representation contained in the [REDACTED] Letter. The Tribunal unhesitatingly answers this question in the negative.
276. The first element to be noted is that the [REDACTED] Letter was given and received in good faith by the Respondent and the Banks respectively. It must therefore be assumed that the Respondent considered itself to be and to remain in a position materially to influence, if not actually to bring about, the result desired by the Banks under the Payment Agreement in accordance with the [REDACTED] Letter; and implicitly the Respondent so represented itself to the Banks.
277. The second element is that the Banks were to receive under the Payment Agreement, not later than 30 September 1993, as security for ESVA's loans and for the fulfilment of Ookean's obligations under the Payment Agreement, first priority mortgages on six vessels of RAS Ookean in a form and substance acceptable to the Banks<sup>61</sup>.
278. This commitment was not honoured by RAS Ookean timeously. Its delays continued until 15 July 1994. There was no good commercial reason for this non-compliance with the Payment Agreement. The Respondent contended that this delay was caused by the Banks' own misconduct but, as will appear below in Part VIII, the Tribunal disagrees.
279. RAS Ookean should have done much more to have the mortgages registered earlier. It did not do this for an improper motive, namely to put further unfair pressure on the Banks to make more concessions in still further negotiations.<sup>62</sup> There is no evidence that the Respondent attempted to curtail RAS Ookean's recalcitrant conduct.
280. Moreover, the vessels which were to be mortgaged were not sold by RAS Ookean until later; and the proceeds were not used to repay the Loan, in spite of what was

---

<sup>61</sup> Article II, 4 of the Payment Agreement.

<sup>62</sup> Mr [REDACTED] Testimony, Transcript, p. 526; Mr [REDACTED] Testimony, Transcript, pp. 1145 and 1146.

agreed in the Payment Agreement<sup>63</sup>. Also, the timetable in Article II, 5 of the Payment Agreement was not observed by RAS Ookean. When RAS Ookean did not do what it had to do under the Payment Agreement, the Respondent did not do anything about it. To the contrary, it took the Respondent a long time to grant the official permits for the mortgage and sale of the vessels.<sup>64</sup>

281. Nonetheless, the Tribunal does not regard the Respondent's conduct so far as a breach by the Respondent of the FET standard in the BITs. That would elevate the status of the [REDACTED] Letter to a guarantee or indemnity, legal characteristics which it never bore. Moreover, the Banks, ever patient, generally acquiesced in the overall delay - up to October 1995.
282. The position changed on 20 October 1995 with the filing in the Tallinn City Court by RAS Ookean of its formal request to have the Payment Agreement and Mortgage Contract declared invalid. The Board of RAS Ookean thereby confirmed that it would not exercise its rights and powers in such a manner so as to ensure that RAS Ookean complied with the obligations contained in the Payment Agreement. Judged by any commercial standards, this was an act of gross bad faith by RAS Ookean towards the Banks, which was not remotely justified. It was also the culmination over many months of deliberate non-performance of the Payment Agreement by RAS Ookean. This litigation, as recited above, challenging the Payment Agreement and Mortgage Contract was nonetheless successful before the Estonian Supreme Court many years later, in November 2001.
283. From the outset, the Respondent not only tolerated but indeed encouraged this litigation for the benefit of RAS Ookean and to the detriment of the Banks. In the Tribunal's view, the Respondent's conduct (not being limited to impassive observation) was a violation of the legitimate expectation created by the [REDACTED] Letter. Taking into account the long history of the Banks' difficulties, the Respondent's conduct was neither even-handed nor fair; and it was utterly

---

<sup>63</sup> Art. II, 3.

<sup>64</sup> See also Mr [REDACTED] Testimony, Transcript pp. 1441 and 1442.

inconsistent with the [REDACTED] Letter. Accordingly, the Respondent violated the FET standard of the Estonia-Germany and Estonia-Finland BITs.

284. In the Tribunal's view, that violation of the latter FET standard by the Respondent began no later than 20 October 1995; and it continued, uninterrupted, up to at least 16 November 2001. As described earlier in Part II of this Award, the history of this litigation is long and complicated. After the decision of the Tallinn City Court of 28 August 1996, a number of appeals and other legal skirmishes occurred. The final decision was issued by the Supreme Court on 16 November 2001. Accordingly, the violation by the Respondent of the Estonia-Finland BIT continued after the entry into force of the Estonia-Germany BIT on 12 January 1997.
285. For the purpose of this part of the Award, it suffices to stop the Tribunal's reasoning at this point, without separately deciding other matters raised by the Banks in support of their case. Accordingly, the Tribunal does not need to decide whether, as the Banks contended, the Respondent's wrongful conduct also amounted to a violation of the BITs as regards full security and protection, the observation of commitments, nationalisation and expropriation. By way of final clarification, the Tribunal does not attribute to the Respondent any act alleged by the Banks to be an international wrong committed by the Respondent's judicial, legislative or other organs, other than its executive based on the [REDACTED] Letter as decided above under the FET standard in the two BITs.



**PART VIII: ISSUE 3 - DID THE BANKS FRUSTRATE THE BARGAIN?**

286. The Respondent submitted that the Banks failed to uphold “their end of the bargain”, thereby disentitling them to any relief on the merits of their claims in these arbitration proceedings.
287. The Respondent contends that the Banks had assured RAS Ookean that it could participate in the new ESVA (*i.e.* Paljassaare). In consideration for agreeing to make payments to the Banks under the Payment Agreement, RAS Ookean was, according to Article V of that Agreement, to obtain from the Banks their rights to the bankruptcy estate of ESVA, proportionately to the payments RAS Ookean would make to them under the Agreement. However, the Respondent submits that the Banks did everything to prevent RAS Ookean from participating. They transferred all of ESVA's estate, but not its debts, to Paljassaare, which was a vehicle of its own making, for a fraction of its value and an ostensible payment by interest-free bonds spread over eight years. According to the Respondent, the Banks' misconduct caused RAS Ookean to invalidate the Payment Agreement.
288. The Respondent adds that, for its part, RAS Ookean complied with the Payment Agreement by selling one of the six vessels in February 1995. It also obtained permission from the Estonian Ministry of Economy to comply with the Payment Agreement.
289. As already indicated, the Tribunal does not accept the Respondent's case that RAS Ookean complied properly and timeously with its obligations under the Payment Agreement (if valid). As regards the Banks' alleged misconduct, the Tribunal does not accept the Respondent's case for the following reasons.
290. When ESVA met financial difficulties and was eventually placed into bankruptcy, the shareholders (the Banks and Valio) decided to sell the company and sought to obtain as good a price as possible. They eventually decided to have ESVA's assets transferred to a new company (Paljassaare) and to try to sell that company, or its assets, to a third party<sup>65</sup>. There is no cogent evidence that this transaction

---

<sup>65</sup> Mr [REDACTED] Testimony, Transcript pp. 218 *et seq.* Mr [REDACTED] Testimony, Transcript p. 921.

was illegal under Estonian law or that it caused any problems with the trustees in ESVA's bankruptcy (or otherwise)<sup>66</sup>. Thus, there is no evidence that the Banks and Valio acquired or sold, through Paljassaare, the ESVA assets for a fraction of their value.

291. Later a plan was made to have RAS Ookean participate in the new company. That could be realised by RAS Ookean taking over the Banks' share against payment of the balance of the Loan. However, in the light of the available evidence, it remains unclear to the Tribunal how closely these two items were directly linked (if at all), let alone the fact whether Ookean would acquire control over the old or the new ESVA was a condition for the repayment of the outstanding Loan. As Mr [REDACTED] testified, these were two different issues<sup>67</sup>. It is significant that the Payment Agreement does not mention any condition of this kind.
292. Further, Ookean did not have the financial means to buy the requisite shares in the new ESVA<sup>68</sup>. It was experiencing grave financial problems<sup>69</sup>. It could not repay the outstanding Loan; and, ultimately, Ookean appeared to lose interest in the establishment of Paljassaare<sup>70</sup>. Several witnesses also testified that Ookean and the Respondent itself were aware as to what was going on with regard to the establishment of Paljassaare and the proposed transaction involving the Banks<sup>71</sup>. There is no evidence that either of them took any action.
293. Thus, there is no sufficient evidence that the acquisition of the Banks' share in ESVA, old or new, was a condition of the Payment Agreement or that it was because of the Banks' misconduct with regard to Paljassaare (and the transfer of assets from ESVA to Paljassaare) that Ookean did not comply with its obligations under the Payment Agreement. On the contrary, as mentioned already, there is cogent evidence that the delay that occurred in establishing the mortgages on the

---

<sup>66</sup> Mr [REDACTED] Testimony, Transcript pp. 334-335.

<sup>67</sup> Transcript pp. 938 and 985; see also Mr [REDACTED] Testimony, Transcript p. 321; Mr [REDACTED] Testimony, Transcript p. 529.

<sup>68</sup> Mr [REDACTED] Testimony, Transcript p. 999.

<sup>69</sup> This is clear from the evidence in general, but see also Mr [REDACTED] Testimony, Transcript pp. 252, 318 and 324; Mr [REDACTED] Testimony, Transcript p. 497: "*we were in direct need of money*".

<sup>70</sup> Mr [REDACTED] Testimony, Transcript p. 660.

<sup>71</sup> Mr [REDACTED] Testimony, Transcript p. 1008, [REDACTED] Testimony, Transcript p. 668.

six vessels was nothing else than an attempt to put further unfair pressure on the Banks<sup>72</sup>.

294. The Tribunal, in the light of these several considerations, does not accept the Respondent's case that it was the Banks' own conduct that frustrated the proper and timely implementation of the Payment Agreement by RAS Ookean. Accordingly, the Tribunal rejects this part of the Respondent's defence.

---

<sup>72</sup> Mr [REDACTED] Testimony, Transcript p. 526; Mr [REDACTED] Testimony, Transcript p. 1145-46.

## ***PART IX: ISSUE 4 - DAMAGES***

### ***(A) Introduction***

295. Having determined that the Respondent violated the FET standard in the two BITs, the Tribunal now considers the Banks' claims for damages resulting from such breach.
296. For reasons appearing below, it is necessary for certain purposes to distinguish between the First and Third Claimants claiming under the Estonia-Finland BIT and the Second Claimant claiming under the Estonia-Germany BIT.

### ***(B) The Banks' Position***

297. In their Memorial the Banks claim that, as a direct result of the Respondent's breaches of the BITs, the Banks lost their investment in Estonia and suffered a considerable amount of losses in the form of lost capital gains, as well as additional costs and expenses incurred while trying to resolve this dispute.
298. The Banks submit that the compensation to be awarded should be determined on the basis of the general principles of international law. In accordance with the widely accepted principle of *restitutio in integrum*, the Respondent should be held liable to pay compensation for its breaches so that all the consequences of its unlawful conduct are wiped out and the current situation corrected to resemble, as far as possible, the situation that the Banks would be in today, had the Respondent lived up to its obligations under the BITs. Absent the Respondent's breaches, the Banks would have received back the investment secured by Estrôbprom's Guarantee, as well as interest (both regular interest and default interest) under the Loan Agreement.
299. With regard to interest, the Banks further submit that, due to the Respondent's breaches, their investment and its profit (*i.e.* interest) have not been at the Banks' disposal and that, therefore, the Banks have also been deprived of their possibility

to reinvest these monies. This also applies to default interest accrued over the years under the Loan Agreement. Such compensation should, therefore, be awarded by the Tribunal in the form of compound interest.

300. With regard to the principal amount, the Banks submit that the total principal amount paid by the Banks to ESVA under the Loan Agreement during the years 1989 and 1990 was USD 7,565,485.32 and DEM 26,794,081.60; and that this principal amount developed thereafter as follows:

(1) ESVA repaid USD 15,076.54 and DEM 44,053.83 in 1992;

(2) At the time of the Notice of Termination on 16 December 1992, the unpaid principal thus amounted to USD 7,550,408.78 and DEM 26,750,027.77, interest according to the Loan Agreement to USD 48,232.60 and DEM 431,254.46 and default interest to USD 15,838.75 and DEM 87,110.31;

(3) After the Notice of Termination in 1992, the Banks received Valio's payment under its Guarantee, totalling 48 % of the Loan;

(4) The outstanding balance of the Loan attributable to Estrôbbprom's Guarantee at the time of the Notice of Termination was thus USD 3,959,529.67 and DEM 14,179,564.12, which is what the Banks claim as the outstanding principal amount of damages, together with contractual interest according to the Loan Agreement.

301. The proceeds from the sale of the "Heinaste" have not been taken into account when calculating this outstanding balance because this amount was later returned to the bankruptcy estate of Ookean by the Banks pursuant to the judgment of the Supreme Court of Estonia.

302. On this principal amount, the Banks primarily claim default interest to be determined on the basis of the Loan Agreement from the date of the Notice of Termination on 16 December 1992 until the date of the Supreme Court's decision on 16 November 2001, this date being the date on which it became evident that RAS Ookean was not going to pay the balance receivable under the Loan

Agreement and the Guarantee. (As regards the calculation of the Banks' interest claim, these sums are taken into account separately below).

303. In this regard, the Banks submit that, pursuant to Article 10 of the Loan Agreement, the Banks are entitled to default interest of 2% per annum above the rate applicable to the overdue amount immediately prior to the due date. As the rate applicable to the amount due on the date immediately prior to the Notice of Termination (as evidenced by the Notice of Termination) was 3.8125% on the principal amount in US dollars and 9.625% on the principal amount in German marks, the default rate should be calculated using interest rates of 5.8125% for the USD sum and 11.625% for the DEM sum, compounded annually.
304. The Banks further submit that, in 1994, the Banks received the equivalent of USD 307,362.59 and DEM 1,070,435.66 as advance dividends from ESVA's bankruptcy estate. The Banks submit, in their Memorial, that these dividends have been deducted from the default interest accrued until the date of payment of these dividends. The development of the amount under this heading until 16 November 2001 amounts to USD 2,156,672.47 and DEM 21,583,748.76.
305. After 16 November 2001, the Banks contend that the interest rate should be awarded in accordance with a generally accepted level. The Banks submit that an interest rate of 6 % per annum, compounded annually, corresponds to the established decisions of previous ICSID tribunals and should be considered as an equitable compensation for the Banks' inability efficiently to use these monies. The Banks add in their Memorial that, in reality, the Banks would have been most likely, due to their line of business, to have received a profit greater than 6% per annum if the monies have been available for them to reinvest.
306. As already noted above, the Banks received final dividends from ESVA's bankruptcy estate in the amounts of DEM 4,072,154.46 in September 2002, DEM 1,035,337.63 in November 2002 and DEM 124,214.70 in December 2002. The final dividends have been taken into account as a deduction of the default interest incurred on this amount since the date of payment of the dividend.

307. The sum of the default interest claimed by the Banks under this heading is USD 3,199,656.78 and DEM 21,897,728.82, as at 15 July 2004.
308. Alternatively, and as a secondary claim, the Banks submit that the default interest on the principal amount and interest should be calculated at an annual compound rate of 6% per annum as from the Notice of Termination until the date of payment (subject equally to a deduction for the dividends described above). The amount of such default interest as at the date of the Banks' Memorial is USD 3,316,678.14 and DEM 6,130,097.25.
309. In addition, the Banks claim, in their Memorial, an amount of EUR 1,200,000.00 for expenses incurred before these arbitration proceedings (legal fees, stamp duties, time spent by in-house counsel), and the return of USD 622,143.32 representing the "Heinaste" sale proceeds.
310. For these amounts, the Banks also claim compound annual interest at the rate of 6% per annum, with the following commencement dates:
- (1) For the expenses and costs: from the date that the reimbursement of these costs and expenses was claimed from the Respondent, *i.e.* the date of the Notification of a Claim of 30 August 2002; and
  - (2) For the additional sum returned to the estate of RAS Ookean: from the date the payment was made, *i.e.* 20 February 2002.
311. The Banks submit that German marks have been used in the calculations after the adoption of the European single currency (EUR). Only the sum of the amounts has been converted to Euros.
312. Finally, the Banks claim compensation for all the expenses and fees incurred by the Banks in connection with these arbitration proceedings, together with interest, and that the Respondent should bear all the expenses and fees of the arbitration proceedings, including the fees and expenses payable to the Arbitrators.

***(C) The Respondent's Position***

313. In its Counter-Memorial, as well as its Rejoinder, the Respondent disputed the methodology adopted by the Banks for the quantum of their damages; and the Respondent raised a number of further objections in correspondence after the Hearing, notably in the Respondent's letters of 16 February and 1 March 2006.
314. First of all, however, the Respondent submits that the Banks' claim for damages must fail for lack of legal nexus and causation. It submits that the Banks' claim damages for the loss of their Loan; and since this Loan, according to the Respondent, cannot be considered as an investment in Estonia, that claim must fail. The Tribunal has already addressed this argument as a jurisdictional issue (in Part VI of this Award above) and rejected it; and the Tribunal rejects it here for the same reasons.
315. With regard to the amount claimed, the Respondent submits that, for the principal compensation, the maximum to which the Banks could be entitled would be equal to the market value of the six ships to be sold under the Payment Agreement. They argue that, in reality, the Banks' only putative asset in Estonia which could conceivably fall within the scope of the two BITs and the ICSID Convention are the Banks' rights under the Payment Agreement. Thus, the Respondent submits that it is only in respect of those rights, not the Loan or Loan Agreement or Guarantee, that the Banks may seek compensation in these proceedings, provided of course that the Tribunal were able to make a finding that the Payment Agreement was valid and enforceable under applicable Estonian law and that the Respondent was liable for its non-fulfilment.
316. With regard to the Banks' methodology on the principal amount, the Respondent principally submitted, in its Counter-Memorial and its Rejoinder, the following:
- (1) It is uncertain whether the amount claimed by the Banks fully reflects the amounts received as dividends in ESVA's estate (a total of USD 5.6 million); and
  - (2) The refund of the amount of USD 622,143 related to the "Heinaste" (*i.e.* the difference in the purchase price and the documented sale price which the Banks



- had to repay after the Payment Agreement and the Mortgage Contract were declared invalid by the Estonian Supreme Court) should be refused, as the Banks failed to prove, in the Estonian Courts, why the amount realised was USD 622,143 less than the amount expressly stated in RAS Ookean's written agreement for the "Heinaste".
317. In its Closing Submission, the Respondent stated that the Banks' claim should be limited to what they might have recovered in the Ookean bankruptcy, as unsecured creditors.
318. With regard to the interest claimed, the Respondent principally submits the following:
- (1) No default interest is due, or at least not for a period of thirteen years over which such interest is claimed by the Banks. The Respondent submits that to bear a debtor's default for a period of thirteen years is manifestly unreasonable. In its submission, default interest in a loan contract is a means of forcing payment of an undisputed debt, which in practice either leads to prompt payment or to prompt insolvency of the debtor;
  - (2) The Payment Agreement has no provision on interest;
  - (3) Unlike several national laws, international law does not provide for a fixed or generally accepted interest rate. On the contrary, the rule is that a tribunal must evaluate all the relevant circumstances in determining the rate of interest, if any;
  - (4) Interest should start to run on the date of the submission to arbitration of the international law claim (this being the date on which "the state's international responsibility became engaged"); in this case, that is the date of the Banks' Request for Arbitration of 10 December 2003; and
  - (5) Compound interest (as opposed to simple, compensatory interest) is in principle not allowed in international law.
319. In its Counter-Memorial, the Respondent also disputed the Banks' claim for costs and expenses in connection with court proceedings in Estonia and South Africa.

The Respondent's principal objection against the Banks' claim is that these costs relate to litigation and that these costs should therefore be considered as having been incurred in the Banks' regular course of business. Notably, the Respondent principally submits:

(1) The litigation costs were incurred in the Estonian Courts (a forum to which the Banks expressly agreed in the Payment Agreement), and in the South African Courts (a forum to which the Banks chose to resort);

(2) These costs were incurred in litigation not with the Respondent but with RAS Ookean; and

(3) The litigation costs related to the Payment Agreement and the Mortgage Contract, not to the Banks' alleged investment under the BITs.

320. The Respondent also disputes the amount claimed of USD 1.2 million.

321. The Respondent finally asserts that the Banks, at some point in time, were prepared to accept USD 1.13 million in amicable settlement of their whole claim.

***(D) The Tribunal's Decision***

322. As already noted immediately above and in Part I of this Award, the Respondent raised certain objections against the Banks' claim in correspondence after the Hearing. It is necessary to deal here with these objections first.

323. The Respondent's letter of 17 March 2006 crossed with a letter of the Tribunal that confirmed that the Tribunal did not wish to receive any further submissions by the Parties. That letter from the Respondent has not therefore been taken into consideration by the Tribunal.

324. The Respondent's other two letters, those of 16 February and 1 March 2006, have been considered by the Tribunal; and they touched upon the following issues regarding quantum:

- (1) As it had done already in its Rejoinder, the Respondent queried whether the Banks' claim fully reflected the amounts received as advance and final dividends in the ESVA bankruptcy estate;
- (2) The Respondent asserted that the price received by the Banks for the sale of their shares in the new ESVA should be deducted from the compensation claimed by the Banks; and
- (3) In the letter of 1 March 2006, the Respondent raised what it called a fundamental question regarding the Banks' claim.
325. The Tribunal has decided not to take the last matter into account. It was not raised in the Respondent's earlier written submissions or at the Hearing. It was notably absent from the Respondent's Opening and Closing Statements. There is no sufficient reason why the Respondent could not have raised this matter, had it wished to raise this question, at the proper time. It would be neither fair to the Banks nor appropriate for the Tribunal under its procedures and orders to accept so late the Respondent's unsolicited new assertion; and the Tribunal declines to do so.
326. With regard to the question whether the Banks took all dividends received from the ESVA estate into account in its Claim, the Tribunal is satisfied, affirmatively, that this was the case. The Banks accounted for these dividends in their Memorial<sup>73</sup>, their Reply<sup>74</sup> and Exhibits C56 and C57 and a statement by Mr ██████████ of 9 March 2006. The Tribunal is satisfied that these parts of the Banks' submissions represent accurately what the Banks in fact received by way of dividends from the ESVA estate.
327. With regard to the proceeds of the Banks' shares in the new ESVA, it appears from the Banks' letter of 20 February 2006 that the price they received for these shares from Moon Holding in 1996 was FIM 48,400.00 to the First Claimant, FIM 48,800.00 to the Third Claimant and DEM 16,000.00 to the Second Claimant or EUR 24,528.54 in total.

---

<sup>73</sup> Memorial of 15 July 2004, para. VI 4.1.1.6/11.

<sup>74</sup> Reply on the merits of 31 January 2005, para. VII 1.17/18.

328. The Banks submit that these amounts should not be taken into account. In their view, the original debtor was ESVA. Hence, only the amount received from ESVA or its bankruptcy estate should be taken into account.
329. The Tribunal disagrees with the Banks' submission. Essentially, the Banks claim compensation for the loss of their investment. This, as explained below, is what the Tribunal generally accepts as the Banks' recoverable compensation. Any amount received by the Banks in connection with that investment should then be deducted from the compensation to be awarded in these proceedings.
330. With regard to the Respondent's principal objections, the Tribunal observes first of all that, as set out above, the Respondent violated the FET standard in the two BITs, resulting in the loss of at least a significant part of the Banks' investment. As a general principle, in the opinion of the Tribunal, the Banks should be put in the same position as if such violations had not occurred.
331. In essence, the Respondent has not materially disputed this general approach. Indeed, in most cases (if not all) where compensation is claimed for a breach of an investment treaty, compensation is awarded on the principle that the injured party should be put in the same situation as if the violation of the treaty causing the injury had not occurred. In the present case, however, the Respondent submits that this approach would be limited to compensation for the six vessels to be sold under the Payment Agreement. Also, as mentioned above, the Respondent submits that, for the principal amount of damages, the maximum to which the Banks would be entitled would be limited to the market value of these six vessels.
332. Insofar as the Respondent rests its argument on the basis that the Banks cannot claim damages at all (as the Payment Agreement was found to be invalid and unenforceable by the Estonian Supreme Court), this is rejected by the Tribunal. Whatever the merits of the decision of the Estonian Supreme Court under Estonian law, the fact remains that the Banks still had (and have) their investment in Estonia and that this investment did not receive from the Respondent fair and equitable treatment in accordance with the BITs. These violations stand by themselves, not being dependent on the ultimate validity of the Payment

- Agreement. In the same vein, the Respondent's argument is rejected that the Banks' claim should be considered as a claim under the Payment Agreement, and therefore not against the Respondent but against RAS Ookean. The Banks' claim is made and here determined against the Respondent under the two BITs and not against RAS Ookean under the Payment Agreement.
333. The Respondent's argument that the Banks cannot claim more than the restitution of the six vessels in kind, or the market value of the six ships to be sold pursuant to the Payment Agreement, is equally rejected by the Tribunal. The Banks' principal investment was the original Loan. A significant balance of that Loan remained unpaid in September 1993. Subject to the general principle of restitution described above, the Banks are entitled to recover full monetary compensation for the balance of this investment, not limited to the value of the vessels under the Payment Agreement. Of course, the Tribunal accepts that the solution for the repayment of the Loan provided in the Payment Agreement was indeed the sale of these six vessels; but this, however, was only the means to have the Banks' outstanding Loan repaid, not thereby limiting the recovery of either the Loan or the investment itself.
334. With regard to the Respondent's submission that the Banks' claim should be limited to what the Banks might have recovered in the Ookean bankruptcy as unsecured creditors, the Tribunal considers that this argument overlooks the fact that, already in September 1993, the Banks could reasonably expect that they would be secured creditors, through the mortgages on the six vessels pursuant to the Payment Agreement or indeed otherwise by litigation in Estonia and elsewhere.
335. In September 1993, there was no reason to believe that the sale of the six vessels would not, as was expected by the parties to the Payment Agreement, have compensated the Banks for the then outstanding balance of their investment. The parties to the Payment Agreement obviously expected that the vessels could be sold at more than their book value. It was up to the Respondent to prove that, in spite of those expectations, this could never have been the case. The Respondent has not produced evidence to this effect in these arbitration proceedings.

336. The Tribunal will not address any alleged settlement negotiations taking place between the Parties: any such private negotiations did not yield any concrete result; they cannot be considered as an admission or concession by the Banks or the Respondent in these arbitration proceedings; and accordingly they should not be considered by this Tribunal at all. Nor have they been so considered.
337. It follows from these observations by the Tribunal that, with regard to the damages suffered by the Banks, the Tribunal considers that the Banks are entitled to damages measured by reference to the balance of the Loan as it existed at the time of the Payment Agreement and the [REDACTED] Letter on 17 September 1993. At that time, the Banks could reasonably believe that their investment, as it then stood, would be repaid. Accordingly, in the opinion of the Tribunal, the measure of damages recoverable by the Banks as a principal amount is the outstanding balance of the Loan plus default interest under the Loan Agreement up to 17 September 1993 as restated in Section A of the preamble of the Payment Agreement.
338. Under the Payment Agreement, default interest would have occurred after that date as well. But that, in the opinion of the Tribunal, is not appropriate for the claim at issue under the two BITs for several reasons. First, the Banks are not claiming damages from its debtor under the Payment Agreement but damages from the Respondent on the ground of the Respondent's violations of the applicable BITs.
339. Second, as set out earlier, the Tribunal has determined that the first breach by the Respondent of its obligations under the relevant BIT occurred when RAS Ookean was permitted or encouraged to start its action to have the Payment Agreement and Mortgage Contract annulled. This means, in the opinion of the Tribunal, that the first breach of obligation under the Estonia-Finland BIT was 20 October 1995. Before that date, the liability of the Respondent did not become engaged under this BIT.
340. Third, the liability of the Respondent under the Estonia-Germany BIT could not become engaged before that BIT's entry into force on 12 January 1997.

341. With regard to the Respondent's objections against the Banks' methodology for calculating the principal amount due to them, with interest, the Tribunal determines the following:

(1) First, the outstanding principal amounts at the time of the Notice of Termination, with interest to that date and the conversion of the DEM sum into Euros, have not been disputed as such by the Respondent (except for the latter's query whether the Banks deducted all dividends which they received from the ESVA estate). As follows from the Tribunal's observations above, the Tribunal's view is that these dividends were properly accounted for;

(2) Second, it is not in dispute that the Banks recovered 48% of the total amount of the Loan then outstanding when Valio paid under its Guarantee; and

(3) Third, the total amount of the Loan outstanding as of the date of the Payment Agreement was set forth in its preamble at Section A.

342. **Damages (Principal Amount):** This means that the Banks' damages as a principal amount, measured as their total unrecovered investment assessed at the time of the Payment Agreement and ████████ Letter on 17 September 1993, amount to USD 4,147,801.49 and DEM 15,441,892.98. Converted into Euros, the DEM portion amounts to EUR 7,895,315.80. These sums (subject to adjustments below) therefore constitute collectively the "principal" amount of damages awarded by the Tribunal required to compensate the Banks for the Respondent's violation of the FET standard under the two BITs.

343. **Compound Interest:** As advanced in the Banks' opening oral submissions at the Hearing, the claim for compound interest was made (*inter alia*) "on the basis of general principles of international law" corresponding to full reparation<sup>75</sup>. The Respondent denies this claim in principle; and accordingly the first question is whether the Tribunal, in the present case, has any power to award compound interest.

---

<sup>75</sup> Transcript p. 80.

344. As a general principle, almost invariably, justice requires that the wrongdoer who has deliberately failed to pay compensation (which it ought to have paid to the claimant) should pay interest over the period during it has withheld that compensation. The claimant, in addition to suffering from the wrongdoing giving rise to compensation, has suffered a further loss from non-payment of that compensation when it should have been paid by the wrongdoer. Moreover, a wrongdoer withholding payment may be unjustly enriched by its deliberate non-payment of such compensation, at the expense of the claimant. In these circumstances, therefore, full reparation will include an order for interest. For a long time, however, liability for interest has been mired in controversy under many national laws, usury being both a sin and a crime in many societies. Significantly, that is no longer so in any of the countries associated with the present case, namely Estonia, Finland, Germany, Sweden and The Netherlands.
345. Yet there may remain something of that controversy attaching to compound interest, as distinct from simple interest, in international law. In Professor Crawford's Third Report on State Responsibility (ILC, 2000), the summary records:<sup>76</sup>
- "[...] although compound interest is not generally awarded under international or by international tribunals, special circumstances may arise which justify some element of compounding as an aspect of full reparation. Care is however needed since allowing compound interest could result in an inflated and disproportionate award, with the amount of interest greatly exceeding the principal amount owed."*
- This caution is perhaps surprising: compound interest reflects economic reality. The time value of money in free market economies is measured in compound interest; simple interest cannot be relied upon to produce full reparation for a claimant's loss occasioned by delay in payment; and under many national laws, an arbitration tribunal is now expressly empowered to award compound interest<sup>77</sup>.
346. The Tribunal has considered the Parties' submissions and their related legal materials. Under international law, the Tribunal concludes that it may order

---

<sup>76</sup> James Crawford, Third report on State responsibility, 4 August 2000, (ILC 2000).

<sup>77</sup> For example, Section 49(3) of the English Arbitration Act 1996 has given arbitrators the power to award compound interest on the principal amount awarded.



compound interest if necessary to ensure full reparation; but that the Tribunal is not required to do so. In reaching these general conclusions, the Tribunal has considered, in particular, Article 38 of the ILC Articles on State Responsibility; Dr F. A Mann QC's article "Compound Interest as an Item of Damage in International Law", in *Further Studies in International Law*<sup>78</sup>; and Judge Schwebel's article "Compound Interest in International Law"<sup>79</sup>.

347. There is a significant convergence between the views of these experienced jurists:  
Dr Mann concluded:

*"on the basis of compelling evidence, compound interest may be and, in the absence of special circumstances, should be awarded to the claimant as damages by international tribunals"*

and Judge Schwebel likewise concluded, more than a decade later:

*"It is plain that the contemporary disposition of international law accords with that found in the national law of States that are commercially advanced, namely, it permits the award of compound interest where the facts of the case support the conclusion that it is appropriate to render just compensation."*

348. It would be otiose to recite here the well-known legal materials considered in these two articles, save to record the position succinctly expressed in the ICSID award in *Santa Elena v Costa Rica*<sup>80</sup>:

*" 103 [...] No uniform rule of law has emerged from the practice in international arbitration as regards the determination of whether compound or simple Interest is appropriate in any given case. Rather, the determination of Interest is a product of the exercise of judgment, taking into account all the circumstances of the case at hand and especially consideration of fairness which must form part of the law to be applied by this Tribunal.*

*104 In particular, where an owner of property has at some earlier time lost the value of his asset but has not received the monetary equivalent that then became due to him, the amount of compensation should reflect, at least in part, the additional sum that his money would have earned, had it, and the income generated by it, been reinvested each year at generally prevailing rates of Interest. It is not the purpose of compound Interest to attribute blame to, or to*

---

<sup>78</sup> F. A. Mann *Further Studies in International Law*, (Oxford Clarendon Press 1990) pp. 377-78, 383-85.

<sup>79</sup> Stephen M. Schwebel, "Compound Interest in International Law" TDM Volume 2, Issue 5, November 2005.

<sup>80</sup> *Compañía del Desarrollo de Santa Elena S.A. v Republic of Costa Rica* (ICSID Case No. ARB/96/1), Award of 17 February 2000, 15 ICSID Rev. - *F.I.L.J.* 169 (2000), 39 ILM 1317 (2000)

*punish, anybody for the delay in the payment made to the expropriated owner; it is a mechanism to ensure that the compensation awarded the Claimant is appropriate in the circumstances.”*

349. This discretionary approach to the award of compound interest under international law may now represent a form of „*jurisprudence constante*“ in ICSID awards. A recent study of 45 ICSID arbitrations resulting in 14 awards of compensation demonstrates that, of the latter, 8 ordered compound interest, 3 simple interest, and 1 no interest (the remaining 2 did not disclose whether compound or simple interest was ordered)<sup>81</sup>.
350. In the present case, the Tribunal considers that full reparation to the Banks should include compound interest on the compensation unpaid by the Respondent when becoming due to the Banks. It would be unjust in these circumstances to order simple interest only, falling significantly short of such reparation. There is also a special “circumstance” in this case which confirms the appropriateness of compound, as opposed, to simple interest: the Banks were and remain financial institutions, in the business of advancing money commercially at compound rates of interest; and the Banks were known as such to the Respondent at all material times. To compensate the Banks for their loss of use of the compensation due to them necessarily requires an order for compound and not simple interest: in losing the use of such compensation after the due date, these Banks suffered that loss at least in terms of compound interest.
351. The position is no different seen from the Respondent’s perspective: if the Respondent wished to borrow monies from any similar financial institution in order to pay the compensation due to these Banks, on commercial terms, the Respondent would have probably incurred compound interest on such borrowings. It is equally probable that the Respondent has therefore benefited unjustly from its non-payment of such compensation, at the Banks’ expense.
352. In the Tribunal’s view, there is nothing in the two BITs that restricts the Tribunal’s power to award compound interest under international law for breach

---

<sup>81</sup> James Gray, Jason Cain and Wayne Wilson, “ICSID Arbitration Awards and Cost”, TDM Volume 3, Issue 5, December 2006.

- of the Respondent's obligations under these BITs. The Tribunal notes the references to "interest" in Article 4(2) of the Estonia-Germany BIT (*"The compensation must be paid without delay and with interest according to the usual interest rates of banks and calculated up to the date of actual payment"*<sup>82</sup>). It is axiomatic that the "usual interest rate of banks" is levied at compound rates of interest, being a banking trade usage in transnational trade.
353. The Tribunal also notes Article 5(1)(c) of the Estonia-Finland BIT: *"The compensation shall include interest until the date of payment at an appropriate commercial rate as determined by the Central Bank of the Contracting Party"*<sup>83</sup>. Whilst this reference might be understood as being limited to simple interest, it appears in a paragraph on the "payment of prompt, adequate and effective compensation". In other words, this reference to interest relates only to a lawful expropriation accompanied by such compensation including interest, timeously paid. It can have no relevance to reparation for an unlawful expropriation where the injury is both an unlawful measure and an unlawful failure to pay any compensation when due. The analogy with a violation of the FET standard speaks for itself.
354. It remains for the Tribunal to make clear what it does *not* here decide. By this decision in favour of compound interest, the Tribunal is not deciding to punish the Respondent. Nor is this decision based upon any national law or the contractual terms of the several instruments at issue in this case, including the Loan Agreement, the Guarantees and the Payment Agreement. The Tribunal does not think it appropriate to apply, as against the Respondent, any of these instruments' express or implied provisions on interest; none of which were contractually applicable to the Respondent under the two BITs; and, in its view, the Banks are fairly compensated in this case by the award of compound interest under international law, without any unfairness to the Respondent.
355. With regard to the rate of compound interest to be awarded, the Tribunal refers to its observations above that its decision to award compound interest is not related

---

<sup>82</sup> This is the English translation of the original German and Estonian original versions.

<sup>83</sup> This is the original text of the English version, equivalent to the Finnish and Estonian versions.

- to any contractual interest in this case but to the Tribunal's general acceptance of compound interest, in this particular case, as a proper means of compensation under international law. In that light, and since it was not disputed by the Respondent that a rate of 6% per annum (compounded annually) is not in itself an abnormal rate over the relevant period, the Tribunal will apply this rate.
356. As regards the commencement date for compound interest, it would be invidious in this case to distinguish between the Banks and the two BITs. For this reason, the Tribunal is unwilling to fix 20 October 1995 in regard to the Estonia-Finland BIT; and there could be no logic in fixing 12 January 1997 in regard to the Estonia-Germany BIT. In all the circumstances, under the exercise of its broad discretionary powers, the Tribunal decides to fix 16 November 2001, being the date when the Estonian Supreme Court finally declared the Payment Agreement and Mortgage Contract invalid<sup>84</sup>.
357. Accordingly, in addition to the principal amounts as damages set out above in paragraph 342 of this Award (subject to adjustments below), the Tribunal awards interest from 16 November 2001 at the rate of 6% per annum compounded annually until 15 November 2007. The Tribunal thus awards interest in the amount of USD 1,606,193.27 and EUR 3,063,692.07. Subject to adjustment of the amount in Euros as set out below, the Tribunal awards that these sums shall bear interest from 16 November 2007 at the rate of 6% per annum compounded annually until payment.
358. *The ESVA Proceeds*: As stated above, any amount received by the Banks in connection with their investment should be deducted from the compensation to be awarded. The Tribunal finds that the Banks have shown sufficient evidence in regard to the proceeds received from the ESVA estate. Deductions should thus be made for sums received by the Banks in 1994, 1996 and 2002.

---

<sup>84</sup> A minority of the Tribunal has a different view. A minority is of the opinion that interest should be awarded, on the principal amount due, from the date that the litigation started for the first and third Claimant and from the date the Estonia-Germany BIT entered into force for the second Claimant.

359. As regards the sums received in 1994 (“advance dividends” or “advance payments”<sup>85</sup>) and in 1996 (proceeds from the sale of new ESVA to Moon Holding<sup>86</sup>) the Tribunal decides that these sums (the “ESVA 1994/1996 proceeds”) should be deducted from the amounts set out in paragraph 342 of this Award.
360. The information provided by the Banks has not been fully consistent with regard to the ESVA proceeds. The 1994 sums listed in Exhibits C 56 and C 57 to the Banks' Memorial are set out in USD and DEM, while a subsequent statement by Mr [REDACTED] dated 9 March 2006 lists sums in EEK, includes payments made to Valio Oy and differs as to the date of one of the payments (5 May 1994 instead of 1 March 1994). As the Banks have not provided any exchange rate in regard to the 1994 EEK amounts in Mr [REDACTED]'s statement, the Tribunal decides to round upwards the amounts in Exhibits C 56 and C 57, with the DEM converted to Euros. The Tribunal also decides to add EUR 25,000 to the EUR amount portion deduction in respect of the proceeds received from Moon Holding. Under its discretionary powers, the Tribunal thus decides to deduct a lump sum of USD 310,000.00 and EUR 575,000.00 from the amounts set out in paragraph 342 of this Award.
361. Accordingly, the Banks' damages as principal amounts after these deductions amount to USD 3,837,801.49 and EUR 7,320,315.80. So far as the claims of the First and Third Claimants are concerned (under the Estonia-Finland BIT), they are thus entitled to compensation respectively in the sum of USD 1,279,267.10 and EUR 2,440,105.20 each being one-third of the total damages awarded. So far as the claims of the Second Claimant are concerned (under the Estonia-Germany BIT), it is likewise entitled to compensation in the sum of USD 1,279,267.10 and EUR 2,440,105.20, again being one-third of the total damages awarded.
362. As regards the sums received in 2002 (dividends, the “ESVA 2002 proceeds”), the Tribunal decides to depart from the information provided in Mr [REDACTED]'s statement of 9 March 2006, *i.e.* to deduct only those amounts, specified in Euros,

---

<sup>85</sup> See Section VI.4.1.1.6 of the Memorial and the Statement of [REDACTED] of 9 March 2006.

<sup>86</sup> See Claimants' letters of 20 February 2006 and 10 March 2006.

- paid to the Banks. Mr. [REDACTED]'s statement lists that the Banks received (i) EUR 1,342,030 on 6 September 2002; (ii) EUR 341,208.61 on 26 November 2002; and (iii) EUR 40,943.99 on 18 December 2002. The Tribunal decides that these sums with interest at the rate of 6% per annum compounded annually from each of the dates on which the distributions were made until 15 November 2007 should be deducted from the EUR portion of the compound interest awarded on the principal amounts as damages as decided under paragraph 357. According to the Tribunal's calculation, the ESVA 2002 proceeds with interest amount to EUR 2,326,809.57 (EUR 1,816,410.74, EUR 455,885.73 and EUR 54,513.10).
363. Accordingly, in addition to the principal amounts as damages under paragraph 342 of this Award as adjusted under paragraph 361 of this Award, the Tribunal awards interest in the amount of USD 1,606,193.27 and EUR 736,882.50 (EUR 3,063,692.07 deducted by EUR 2,326,809.57) as at 15 November 2007. These sums are to bear interest from 16 November 2007 at the rate of 6% per annum compounded annually until payment.
364. ***The "Heinaste" Proceeds:*** The Respondent also disputes that the Banks are entitled to a refund of the USD 622,143.32, being the proceeds of the sale of the "Heinaste" (which the Banks had to repay after the Payment Agreement and the Mortgage Contract were declared invalid). However, the Respondent does not dispute that this amount was in fact first received and then repaid by the Banks, and that it was not included in the balance of the outstanding Loan calculated by the Banks as at 16 December 1992 (being the Notice of Termination). The Banks are therefore entitled to further compensation in respect of this sum, together with interest as separately decided below.
365. ***Expenses:*** The Respondent's principal objection against the Banks' claim of EUR 1,200,000.00 for the expenses incurred before this arbitration is that these costs relate to the litigation in the Estonian Courts (and elsewhere) and that these costs should be considered as having been incurred in the Banks' ordinary course of business.

366. This argument is rejected by the Tribunal. All these costs were reasonably incurred and related to the Banks' efforts to get their investment repaid, directly or indirectly. If the investment had been properly protected by the Respondent under the BITs, these costs and expenses would either not have been incurred or would have been recovered from RAS Ookean and its assets. Thus, such costs are part of the damages for which the Respondent is liable, as determined above. The Tribunal therefore accepts the amounts claimed by the Banks as further compensation, together with interest as decided separately below.
367. ***Further Compound Interest:*** For the same reasons described above, the Tribunal awards interest on the two principal sums above, namely USD 622,143.32 and EUR 1,200,000.00, at the rate of 6% per annum compounded annually until the date of payment, as from 20 February 2002 for the first sum (USD 622,143.32) and as from 30 August 2002 for the second sum (EUR 1,200,000.00), to be paid in equal shares to the Banks.

## ***PART X: LEGAL AND ARBITRATION COSTS***

368. The Tribunal has made its decisions in favour of the Banks on both liability and quantum. Accordingly, subject to special factors indicating otherwise, the Tribunal determines that the Banks are entitled to compensation for their reasonable costs incurred in these arbitration proceedings as the successful party. The Respondent also claimed costs, as specified in its submission of 8 March 2006. The Tribunal rejects the Respondent's claim in principle, in the light of the Tribunal's decisions above: as the unsuccessful party, the Respondent is not entitled to payment of any costs from the Banks.
369. As a special factor, the Respondent submitted that the Banks are not entitled to costs because their conduct unnecessarily complicated these arbitration proceedings. The Tribunal does not accept this criticism of the Banks. To the contrary, the Banks presented their case in a straightforward and professional manner. In the Tribunal's view, there are no other special factors in this case which could determine as a matter of principle that the Banks should not recover their costs from the Respondent (subject to their amount) as the successful party.
370. In their letter of 8 March 2006, the Banks claimed costs in the amount of EUR 1,815,785.37, comprised of the following items (excluding VAT):
- (i) Fees and costs of Hannes Snellman Attorneys at Law Ltd., to a principal amount of EUR 1,589,659.10;
  - (ii) Fees and costs of OY Asianajotoimisto Hedman Osbourne Clark Advokatbyrå Ab, to a principal amount of EUR 104,018.60;
  - (iii) Fees and costs of Law Office Tark & Co, to a principal amount of EUR 45,839.00;
  - (iv) Compensation for the time spent on the case by Mr [REDACTED] and Mr [REDACTED] (General Counsel for OKO) and other in-house counsel of the Banks to a principal amount (estimated) of EUR 35,000.00;



- (v) Compensation for the time spent, costs accrued and witness fee of Mr [REDACTED] to a principal amount of EUR 17,750.40;
- (vi) Compensation for the time spent, costs accrued and witness fee of Mr [REDACTED] to a principal amount (estimated) of EUR 13,000.00; and
- (vii) Costs paid directly by OKO Osuuspankkien Keskuspankki Oyj, to a principal amount of EUR 10,518.19.

On items (i), (ii), (iii), (v) and (vii) the Banks provided a break-down of costs.

371. In addition, the Banks requested the Tribunal to order the Respondent to bear the expenses and fees of the arbitration proceedings including the fees payable to the arbitrators. The Parties' advances to ICSID to cover the costs of the arbitration amounted to USD 410,000.00 at the closure of the proceedings. The Banks contributed half of this amount, *i.e.* USD 205,000.00.

372. In its comments of 17 March 2006, the Respondent submitted, in summary, that:

- (1) Item (i) exceeds the Respondent's costs of legal assistance by Freshfields Bruckhaus Deringer by ±152% (± EUR 1,5 million as against ± EUR 600,000); and
- (2) Likewise, the cost of the Banks' Estonian law experts exceed those of the Respondent considerably (whereas the latter prepared more reports);
- (3) Mr [REDACTED] spent less time for the preparation of his witness statement and oral testimony than for his other legal work for the Banks;
- (4) There should be no compensation for the work prepared by in-house counsel, and that item almost certainly also covers time devoted to the Estonian legal proceedings;
- (5) Mr [REDACTED]'s and Mr [REDACTED]'s charges are unwarranted; and
- (6) In general, the costs incurred by the Respondent are much less.

373. The Tribunal bases its decision on four particular factors: First, it does not appear from the available evidence that any of the costs claimed by the Banks were not incurred and paid or payable as a matter of fact. This suggests that the Banks, at the time when they had to incur these costs themselves, considered the same to be reasonable and necessary, because there could then be no certainty whether the Banks would ever be able to recover such costs from the Respondent. Second, it is always difficult to compare costs incurred by different Parties. For example, one party may have made a special arrangement with its legal representatives which the other party may not have made. Thus, the mere fact that one party has incurred less costs than the other party does not mean that the latter's higher costs should be considered unreasonable or unnecessary. Third, the Tribunal has no evidence that the costs as claimed by the Banks were unreasonably incurred or unreasonable in amount. The available evidence suggests the contrary; and as a matter of principle, the Tribunal considers that recoverable costs can include reasonably incurred costs for relevant and necessary work performed by in-house counsel. Fourth, whilst the Banks' claim has ultimately succeeded, the Banks' case did not prevail on every legal and factual issue of alleged liability and quantum - far from it. This last factor requires an adjustment downwards to the quantum of the Bank's legal costs.
374. For all those reasons, the legal costs as claimed against the Respondent by the Banks shall be awarded to them in the total sum of EUR 1,500,000.00. The Tribunal also awards interest on this sum as claimed by the Banks in their relief, at the rate of 6% per annum compounded annually until payment.
375. Considering the above-mentioned factors, the Tribunal concludes that it is also appropriate that the costs of the proceeding, *i.e.* the fees and expenses of the Tribunal and the ICSID Secretariat in the total sum of USD 410,000.00, be borne by the Respondent. As the Banks' relief did not include a claim for interest on the costs of the proceeding, this amount shall not bear any interest.

***PART XI: THE OPERATIVE PART***

376. For the reasons above, the Tribunal awards and orders as follows:
1. The Tribunal has jurisdiction over the dispute submitted in this arbitration and the Claimants' claims, as here decided;
  2. The Respondent violated its obligations to accord to the investment of the Claimants fair and equitable treatment in accordance with the Estonia-Finland and Estonia-Germany Bilateral Investment Treaties, thereby causing loss to the Claimants;
  3. In respect of such violations and losses, the Respondent is liable to pay damages to the Claimants, as follows:
    - (i) Monetary damages in the amount of USD 3,837,801.49 and EUR 7,320,315.80 to be paid by the Respondent to the Claimants in equal shares in the amount of USD 1,279,267.10 and EUR 2,440,105.20;
    - (ii) Interest on the amounts in sub-paragraph (i) above at the rate of 6% per annum compounded annually from 16 November 2001 to 15 November 2007, deducted by the sums set out in paragraph 362 of this Award, in the total amount payable of USD 1,606,193.27 and EUR 736,882.50, to be paid by the Respondent to the Claimants in equal shares in the amount of USD 535,397.73 and EUR 245,627.50;
    - (iii) Interest on the total amount of USD 1,606,193.27 and EUR 736,882.50 awarded under sub-paragraph (ii) above at the rate of 6% per annum compounded annually from 16 November 2007 until the date of

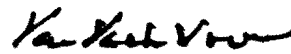
payment, to be paid by the Respondent to the Claimants in equal shares;

- (iv) Monetary damages in the amount of USD 622,143.32 and EUR 1,200,000.00 incurred as expenses by the Claimants prior to these arbitration proceedings, together with the additional sum returned to the bankruptcy estate of RAS Ookean by the Claimants, to be paid by the Respondent to the Claimants in equal shares in the amount of USD 207,381.12 and EUR 400,000.00;
  - (v) Interest on the sums in sub-paragraph (iv) above at the rate of 6% per annum compounded annually until the date of payment as from 30 August 2002 for the amount of EUR 1,200,000.00 and as from 20 February 2002 for the amount of USD 622,143.32 to be paid by the Respondent to the Claimants in equal shares;
  - (vi) An amount of EUR 1,500,000.00 for the Claimants' legal costs in this arbitration, plus interest on this amount as from the date of dispatch of this Award at the rate of 6% per annum compounded annually until the date of payment to be paid by the Respondent to the Claimants in equal shares; and
  - (vii) An amount of USD 205,000.00 for the Claimants' arbitration costs (advances paid to ICSID), to be paid by the Respondent to the Claimants in equal shares in the amount of USD 68,333.33.
4. All payments mentioned above shall be made to the Claimants within sixty days of the date of dispatch of this Award;

5. **Save as ordered above, the Tribunal dismisses all other claims and cross-claims made by the Parties in these arbitration proceedings.**

  
L. Yves Fortier, CC, QC

Date: 14 November 2007



V.V. Veeder, QC

Date: 14 November 2007



O.L.O. de Witt Wijnen

President

Date: 15 November 2007