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# Protecting Swedish investments in Russia through international arbitration

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## Introduction

In response to Russia's military invasion of Ukraine in late February 2022, many countries have acted quickly to impose sanctions on Russia. Unsurprisingly, in the month that has passed since the situation erupted, the Russian government has taken various measures to retaliate against these sanctions and mitigate, at the expense of foreign rights holders, their effects on its market.

Russia's measures target primarily companies with connections to what Russia deems "unfriendly countries"<sup>(1)</sup> (a term used broadly for states that imposed sanctions on Russia and which includes, among others, the United States, the United Kingdom and all European Union member states) and which have ceased their business operations in Russia in opposition to Russia's armed attack on Ukraine.

The measures imposed by Russia may detrimentally affect Swedish companies with operations and investments in Russia in a number of ways. There is a longstanding history of trade and investment between Sweden and Russia. Over 500 Swedish companies have operations or investments in Russia. Certain major Swedish corporations have invested sizeable sums in their Russian markets and provide considerable work opportunities for local communities.

The decisions taken by some of Sweden's largest enterprises to terminate, pause or modify their operations on Russian soil are indeed significant. Such decisions signal a new level of awareness of how business interacts with the geopolitical landscape, much in keeping with the mounting expectations on Swedish companies to act with respect for human rights and exercise leverage with business relationships to ensure partners do too.

However, as seen from the recent barrage of Russian legislative acts, such decisions may have repercussions and companies that have found that they can no longer maintain operations in Russia in current circumstances are likely to be significantly and adversely impacted by the Russian governments' retaliatory measures.

## Brief overview of Russian measures

Matters are evolving rapidly, and new Russian measures have been announced almost daily over the last couple of weeks. Newly enacted or announced legislation targets financial transactions, currency operations, repatriation of assets and IP rights protection. There is also a threat of forced administration, nationalisation and expropriation of assets of companies that are deemed to have ceased their operations in Russia.

Restrictions on transactions involving foreign nationals or companies affect, for example, real estate transactions, credit and loan agreements and transfer of securities<sup>(2)</sup> and prevent foreign companies and individuals from divesting and selling shares and bonds traded on the Russian stock exchange.<sup>(3)</sup> Other measures compel currency conversions into roubles and, significantly, foreign creditors from "unfriendly" states must accept payment of debts in roubles paid into special accounts from which transfers out of Russia or conversion into other currencies are not allowed.<sup>(4)</sup>

The scope of changes to IP protection is yet unclear, but according to Russian media, the enacted and considered legislation is supposed to mitigate the effects of supply chain interruptions, reduce shortages of goods and services resulting from Western sanctions, secure the production of goods and services that would otherwise no longer be available to Russian citizens and facilitate the import of such products from third countries.<sup>(5)</sup> Recently enacted legislation reduces to nil compensation for compulsory licensing related to patents held by persons or businesses associated with "unfriendly countries".<sup>(6)</sup> Compulsory licensing under Russian law is envisaged to apply only in respect of extreme need and for the defence and security of the state and the protection of the life and health of the population, but it is possible that the new legislation may be applied to offset the effects of sanctions and corporate boycotts and enable continued access to certain technologies.

Additionally, Russian authorities have been granted the power to exempt from IP protection, including trademark protection, certain goods or groups of goods to be designated at a later point by the Russian government.<sup>(7)</sup> The envisaged reduction in trademark protection seems more generally intended to reduce boycott-induced shortages and may arguably come to target brands that are no longer available in Russia. The situation may also increase the flow of so-called "grey goods" and counterfeits in the Russian market. Combined with a lack of respect for trademark law, this can lead to negative effects for corporate branding, for example, if substandard goods are distributed under established brands.

Perhaps most alarmingly, reports circulate of a legislative proposal permitting forced administration, seizure and sale of companies that have ceased their Russian operations in opposition to the Russian attack on Ukraine.<sup>(8)</sup> The legislation would reportedly affect companies owned to at least 25% by interests in "unfriendly countries" if they have a book value of more than 1 billion roubles and least 100 employees. The format and duration of forced administration would reportedly differ, depending on whether the company actually terminated its activities after 24 February 2022 or merely took steps to do so, and depending on whether the company is willing to resume operations in Russia.



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The forced administration is ostensibly to ensure business continuity and prevent redundancies and bankruptcies. However, one task of the administration is also to liquidate the foreign-owned company by transferring the company's assets to a new company, whose shares are subsequently sold at public auction, with the condition that the new owner continues operations for at least one year. If there are no buyers, the Russian state will purchase the shares in the new company. The original company will be liquidated and the proceeds from the public auction will (probably) be paid to the owners of the original company after liquidation.

The degree of due process, transparency and fair pricing to be expected in such public auctions is however unclear. Precedents, such as the infamous auction process at issue in the *Yukos* arbitration, are not reassuring. In any event, the market value of such assets at the time of the public auction will likely be significantly lower than their value before the Russian measures – or indeed before the Russian invasion of Ukraine – leaving investors to absorb the difference.

#### **What can Swedish companies do to protect their assets in Russia?**

Swedish companies concerned about their assets in Russia should seek legal advice to examine their options for protecting their physical and intellectual property. They should furthermore be mindful to carefully keep, maintain and secure all relevant written records regarding their investments and ensure that such records are available from outside of Russia. Given the complicated situation that may occur with respect to a potential direct or indirect expropriation of IP rights, companies concerned about their IP portfolio may wish to review ways to protect their trademarks, patent and copyrights with legal counsel.

Should companies be deprived of their Russian assets or otherwise suffer harm from the measures outlined above, there are opportunities to request compensation through international arbitration with the Russian state.

Swedish investments in Russia are protected by the 1995 Sweden-Russia Bilateral Investment Treaty (BIT).<sup>(9)</sup> This instrument promises mutual protection of private investments from one country in the territory of the other. These protections include a prohibition of unreasonable, arbitrary or discriminatory measures by the host state and a prohibition against unlawful expropriation or nationalisation. Expropriation and nationalisation are deemed unlawful if they are not carried out in the public interest, under due process of law, in a non-discriminatory manner and against the payment of prompt, adequate and effective compensation. The BIT also contains a guarantee against arbitrary restrictions on the free movement of capital, which should be freely convertible and transferable. A Swedish company investing in Russia may further have legitimate expectations that Russia acts in accordance with its international obligations on protecting IP rights – for example, under the 1994 World Trade Organization Agreement on Trade-Related Aspects of Intellectual Property Rights.

The various measures imposed or proposed by Russia may very well constitute a breach of these protections. A Swedish investor adversely affected by these measures could have a right, under the BIT's dispute settlement clause, to bring a claim against Russia for breach of the BIT in international arbitration proceedings under the United Nations Commission on International Trade Law (UNCITRAL) arbitration rules. Such proceedings, if successful, could result in an award for damages, entitling the Swedish investor to compensation.

The UNCITRAL arbitration rules also offer opportunities for requesting interim measures to avoid harm that could not be adequately repaired through a subsequent award of damages. While an interim order may have limited enforceability in these circumstances, such orders may generate pressure on states to refrain from implementing measures, as it signals that foreign investors may be willing to enforce their rights through legal recourse.

A favourable award under the BIT could be recognised and enforced under the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, to which Russia is a party, in domestic courts in over 160 jurisdictions. Enforcement may require overcoming certain obstacles such as locating attachable state assets and defeating objections based on sovereign immunity of state property. Companies interested in this route should carefully consider prospects for enforcement already at early stages. In an interesting development in this field, the Swedish Supreme Court, in November 2021, ruled that sovereign wealth fund assets that are managed on commercial terms may be seized for the satisfaction of arbitral awards against the state.<sup>(10)</sup> It may be noted that the Russian National Wealth Fund, which reportedly manages some \$175 billion, was subjected to US economic sanctions following Russia's recognition of the Luhansk and Donetsk separatist republics.<sup>(11)</sup>

#### **Comment**

The situation in Russia appears at risk of history repeating itself from other situations where certain national regimes have targeted foreign companies for political reasons, such as in Venezuela in the early 2000s and in Iran in the 1970s and 1980s. It seems likely that the current measures, if applied, may lead to a considerable number of claims against Russia under relevant trade and investment treaties.

The bringing of an international arbitration against a sovereign state is a considerable undertaking. With accurate valuation of the damage suffered, and where appropriate the assistance of an external arbitration funder providing financing for legal costs, this may, however, be the best recourse for recovery. The Russian courts may be unwilling to give much consideration to claims of foreign companies in the present situation. This is amply illustrated by the very recent judgment of a Russian court in the so-called "*Peppa Pig*" case, where the court dismissed a claim by a UK entity for trademark infringements with explicit reference to the economic sanctions imposed by the United Kingdom on Russia.<sup>(12)</sup> At the very least, Swedish entities with Russian interests should consider international processes as part of their contingency plan and prepare accordingly.

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#### **Endnotes**

(1) Order of the Government of the Russian Federation dated 5 March 2022 No. 430-p.

(2) Decree of the President of the Russian Federation No. 81 of 1 March 2022, "On Additional Temporary Economic Measures to Ensure the Financial Stability of the Russian Federation".

(3) Russian Central Bank Order No. 018-34-3/1202 to Russian credit institutions prohibiting the sale of Russian securities by foreigners, 28 February 2022. At the time of writing, the instruction is not publicly available as it appears it was only sent to Russian credit institutions.

(4) Decree of the President of the Russian Federation No. 95 of 5 March 2022, "On the temporary procedure for fulfilling obligations to

certain foreign creditors".

(5) "The Ministry of Economic Development of Russia discusses the removal of restrictions on the use of intellectual property", *TASS*, 5 March 2022.

(6) Decree of the Government of the Russian Federation No. 299 of 6 March 2022, "On amendments to Clause 2 of the methodology for determining the amount of compensation paid to a patent holder when deciding to use an invention, utility model or industrial design without the patent holder's consent, and the procedure for its payment".

(7) Federal Law No. 46-FZ of 8 March 2022, "On amendments to certain legislative acts of the Russian Federation".

(8) It is thought that this proposal is yet to be published. See for relevant reports of the legislation "[Russia considers nationalizing Western businesses that have closed over Ukraine invasion](#)", *Washington Post*, 10 March 2022, and "[VEB and DIA will be allowed to intercept the management of companies leaving Russia](#)", *Interfax*, 10 March 2022 (as translated from Russian).

(9) [Agreement between the Government of the Kingdom of Sweden and the Government of the Russian Federation on the Promotion and Reciprocal Protection of Investments](#), available in English, Russian and Swedish.

(10) See Maria Fogdestam Agius and Ginta Ahrel, "[Swedish Supreme Court Weighs in on Immunity of Sovereign Wealth Fund Assets Under Central Bank Management](#)", *Kluwer Arbitration Blog*, 7 March 2022.

(11) US government, "[Fact Sheet: United States Imposes First Tranche of Swift and Severe Costs on Russia](#)", 22 February 2022.

(12) "[The Russian Court applied sanctions as a reason for claim dismissal in IP dispute](#)", *The Trademark Lawyer*, 15 March 2022.