

**ITERA INTERNATIONAL ENERGY LLC AND ITERA GROUP NV**  
CLAIMANTS

v.

**GEORGIA**  
RESPONDENT

**ICSID CASE No. ARB/08/7**

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**DECISION ON ADMISSIBILITY  
OF ANCILLARY CLAIMS**

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**BEFORE THE ARBITRAL TRIBUNAL COMPOSED OF:**

Judge Hans Danelius, President  
Professor Francisco Orrego Vicuña (Arbitrator)  
Professor Brigitte Stern (Arbitrator)

**SECRETARY OF THE TRIBUNAL:**

Ms. Natalí Sequeira

**DATE OF DISPATCH TO THE PARTIES: 4 December 2009**

## **I. GENERAL BACKGROUND**

1. The Claimants are Itera International Energy LLC (hereinafter “*Itera*”) and Itera Group NV (hereinafter “*IGNV*”). Itera is a company organized under the laws of the State of Florida, USA, and is wholly owned by IGNV, a company organized in Curaçao under the laws in force in The Netherlands.

2. As of 1996, Itera supplied gas in Georgia to state-owned companies and government entities which accumulated considerable debts to Itera, as a result of deliveries of gas which remained unpaid.

3. According to Resolution No. 1612, dated 27 December 2002, issued by the President of Georgia, the Ministry of Finance was ordered to make funds available for the payment of the debt owed by the Ministry of Fuel and Energy to Itera. The latter Ministry was further directed to ensure the payments to Itera and enter into a debt restructuring and repayment agreement with Itera.

4. Also on 27 December 2002, the Energy Ministry of Georgia and Itera concluded Agreement No. 03-910/02 (hereinafter the “*Debt Restructuring Agreement*”) setting out a general framework for the repayment by Georgian state-owned or state-financed organizations of their debts to Itera.

### **(a) Azot**

5. JSC Azot (hereinafter “*Azot*”) was a Georgian state-owned company which operated a large chemical fertilizer plant in Rustavi. The plant produced a variety of chemical products and had numerous employees.

6. On 21 February 2001, the Rustavi City Court approved the initiation of bankruptcy proceedings against Azot. On 27 July 2001, the same court deferred the opening of bankruptcy proceedings and approved a Rehabilitation Plan for Azot in accordance with Georgian bankruptcy law.

7. As result of the negotiations between Itera and the Georgian authorities in connection with Itera’s purchase of 90% of the shares in Azot, IGNV issued on 17 October 2002 a corporate guarantee for the fulfilment of Itera’s obligations resulting from the purchase. These obligations were specified in a Business Plan set-up for Azot which incorporated the Rehabilitation Plan approved by the court.

8. On 31 December 2002, the President of Georgia issued Decree No. 568 authorizing the privatization of Azot. The Decree provided that the state-owned shares in Azot, amounting to 90% of the total stock, should be transferred to Itera by direct sale for a nominal price of US\$500,000 and that an undertaking by Itera to carry out the Business Plan should be made.

9. On 20 March 2003, in furtherance of this Decree, the Ministry of State Property Administration and Itera concluded a Contract for the sale and purchase of a block of state-owned shares in Azot (hereinafter the “*Sale-Purchase Agreement*”). The Sale-Purchase Agreement provided that the Ministry would transfer 24,979,644 shares (90% of the total stock) to Itera for a nominal amount of US\$500,000. An undertaking to fulfil the obligations under the Business Plan was also included in the Agreement and Itera would pay Azot’s verified and recognized debts within three years. Disputes regarding the Sale-Purchase Agreement were to be referred to the Arbitration Institute of the Stockholm Chamber of Commerce.

10. Also on 20 March 2003, the Ministry of Finance and Itera concluded an Agreement on the repayment of Azot’s debt to the Ministry. A Bill was to be submitted to Parliament in order to provide certain state organizations with funds of GEL22,111,941 (the equivalent of approximately US\$10.2 million) to pay their debts for natural gas to Itera, and Itera would then transfer this amount to the Ministry in payment of Azot’s fiscal debts.

11. On 4 October 2003, Decree No. 503 on the Repayment of Debts was promulgated by the President of Georgia. A debt of GEL 22,111,941 to Itera was acknowledged in the Decree, and the Ministry of Finance was instructed to take measures to pay the debt.

12. On 14 November 2003, the Ministry of Finance, Itera and Azot concluded the negotiations of an Agreement (hereinafter the “*Set-Off Agreement*”) providing that pursuant to Decree No. 503, Itera and Azot had concluded contracts for assignment of claims against natural gas consumers in the total amount of GEL 22,111,941.82, that the Ministry. The Set-Off Agreement also provides that, from the moment of signing the Agreement, the Ministry would lose the right to claim tax indebtedness from Azot in that amount, and that Azot would be deemed to have paid off the tax indebtedness in that amount.

13. In March 2005, the Ministry of Economic Development, dissatisfied with Azot, issued a public tender calling for proposals for purchase of the shareholdings and assets of Azot.

14. In a petition of 25 May 2005 to the Rustavi City Court, the Minister of Finance stated that Azot had not been able to carry out the measures envisaged in the Rehabilitation Plan and had not discharged tax and loan indebtedness owed to the Ministry of Finance. The Minister therefore requested the court to terminate Azot’s rehabilitation regime and resume the bankruptcy proceedings.

15. By Decree No. 211 of 28 May 2005, the Government of Georgia granted the Ministry of Economic Development authority to participate in Azot’s rehabilitation and bankruptcy proceedings as a creditor on behalf of the State.

16. On 30 May 2005, an Agreement was concluded between the Ministry of Economic Development and the Energy Invest Joint Stock Company (hereinafter “*Energy Invest*”). According to this Agreement, the Ministry would petition the court to conduct

bankruptcy proceedings in regard to Azot and then make every effort to conclude a purchase agreement with Energy Invest and to sell Azot's assets to Energy Invest.

17. In an Interlocutory Decision of 6 June 2005, the Rustavi City Court decided, upon the request of the Minister of Finance, to terminate the rehabilitation proceedings and pursue bankruptcy proceedings in regard to Azot.

18. In a writ of 23 June 2005, Itera lodged an appeal against the Interlocutory Decision. The appeal was declared inadmissible on 29 August 2005 by the Appeals Chamber for Civil, Entrepreneurial and Bankruptcy Cases of the Tblisi District Court. Itera lodged a new appeal which, on 23 September 2005, was declared to be unfounded by the Appeals Chamber. The appeal was referred to the Supreme Court of Georgia which, on 28 September 2006, rejected the appeal and upheld the Appeals Chamber's Decision of 29 August 2005.

19. By an Agreement of 22 July 2005, Itera, represented by the Receiver in Bankruptcy, sold Azot's immovable property to Energy Invest.

**(b) Sistema**

20. According to the Debt Restructuring Agreement, Itera would assign to a financial agent selected by the Energy Ministry its claims against the debtors in the amount of US\$46,406,352.30. The Energy Ministry would pay this amount to Itera within seven years from 2003 in quarterly instalments. Disputes relating to the conclusion, fulfilment or termination of the Agreement were to be referred to the Arbitration Institute of the Stockholm Chamber of Commerce. On 20 March 2003, the Ministry of Fuel and Energy designated the state-owned company OOO Sistema (hereinafter "*Sistema*") as financial agent.

21. The dispute between the Parties regarding Sistema is based essentially on the following two documents which, in the Claimants' opinion, were validly concluded agreements but, in the Respondent's opinion, were only draft Agreements not validly concluded between the parties concerned:<sup>1</sup>

(i) The Assignment Contract No. 03-144/03, dated 14 July 2003, between Itera and Sistema in which Itera assigned to Sistema its claims under a certain number of contracts for sale and purchase of natural gas. The debtors were to pay US\$13,564,946.29 to Sistema, while Sistema would pay that amount to Itera over a period of seven years in quarterly instalments. Disputes regarding the implementation of the Contract were to be resolved by way of negotiation or, in the last resort, by arbitration at the International Commercial Arbitration Court of the Chamber of Commerce of the Russian Federation (hereinafter "*ICAC*").

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<sup>1</sup> By using in this Decision the terms "Assignment Contract", "Surety Agreement" and "Sistema Agreements", the Arbitral Tribunal takes no position on whether or not these agreements were legally valid, a matter which, as explained above, is in dispute between the parties.

(ii) The Surety Agreement No. 03-162/03, also dated 14 July 2003, between Itera, the Energy Ministry and Sistema in which the Energy Ministry accepted to be liable to Itera for the fulfilment by Sistema of its obligations under the Assignment Contract to Itera. Disputes were to be resolved by ICAC arbitration.

22. In January 2006, Itera initiated arbitration proceedings before ICAC against the Ministry of Energy which Itera accused of having breached the Surety Agreement. These proceedings are still continuing.

23. On 12 September 2006, the Tblisi City Court, at the request of the Ministry of Finance, found that the Ministry of Energy, when signing the Debt Restructuring Agreement and the Surety Agreement, had not been entitled to do so and therefore decided to nullify these Agreements.

## II. PROCEDURE

24. In a letter of 18 April 2008 to the President of Georgia, the Claimants, referring to their investments in Georgia, stated as follows:

“Itera’s and IGV’s investments have been adversely affected by a series of measures taken by Georgia and its agencies and instrumentalities, starting in early 2004. In particular:

(a) Georgia and its agencies and instrumentalities breached, repudiated and/or purported to invalidate several agreements with Itera, including an assignment agreement signed by the State-owned company OOO Sistema, and a surety agreement signed by the Ministry of Fuel and Industry of Georgia (the *Sistema Treaty Violations*); and

(b) the Ministry of Finance and the courts of Georgia orchestrated the bankruptcy of JSC Azot, a company majority-owned by Itera, in violation of prior express commitments, due process and the requirements of Georgian law, and sold Azot’s assets to a third party (the *Azot Treaty Violations*).”

25. The Claimants submitted that the measures taken were breaches of various provisions of the Treaty between the Government of the United States of America and the Government of the Republic of Georgia concerning the Encouragement and Reciprocal Protection of Investment (hereinafter the “*US-Georgia BIT*”) and the Agreement on Encouragement and Reciprocal Protection of Investments between Georgia and the Kingdom of the Netherlands (hereinafter the “*Georgia-Netherlands BIT*”). They also consented to submit their investment dispute with Georgia concerning the “Azot Treaty Violations” to arbitration before the International Centre for the Settlement of Investment Disputes (hereinafter “*ICSID*”) in accordance with the two BITs.

26. In regard to the “Sistema Treaty Violations”, the Claimants stated as follows:

“Arbitration proceedings initiated by Itera in relation to the Sistema Treaty Violations are currently pending before the International Commercial Arbitration Court of the Chamber of Commerce of the Russian Federation (*ICAC*). Those proceedings were commenced against the Ministry of Energy of Georgia (the *Energy Ministry*) pursuant to the agreed mechanism in the surety agreement. In the ICAC proceedings, the Energy Ministry has argued that Georgia (rather than the Energy Ministry) is

the proper party to the arbitration, and that ICAC lacks competence to consider any dispute involving a state entity. Moreover, the Ministry of Justice has already declared its intention to oppose the enforcement of any ICAC award in Itera's favour.

In light of the positions taken by the Energy Ministry and the Ministry of Justice mentioned above, Itera and IGVN fully reserve their rights to submit additional claims arising out of the Sistema Treaty Violations to ICSID, should our clients' losses not be fully compensated as a result of the ICAC proceedings.

Itera and IGVN are presently ready to submit their claims to ICSID, but would be willing to postpone doing so for a short period of time, upon receiving an early indication of Georgia's willingness to present constructive proposals for the amicable settlement of the dispute.

Specifically, we recognise that parallel ICSID and ICAC proceedings may result in disruption and other difficulties, and would thus be willing to agree with the Energy Ministry to suspend the ICAC proceedings pending the outcome of the ICSID arbitration.

Finally, Itera and IGVN fully reserve all their rights and remedies arising out of the Sistema Treaty Violations and the Azot Treaty Violations. Nothing in this letter should be considered as a limitation of any kind on the facts, evidence or legal arguments Itera and IGVN may present, or on the legal rights and remedies Itera and IGVN may pursue, in support of their claims before the ICAC or ICSID tribunals or otherwise." (Emphasis added)

27. On 5 June 2008, ICSID registered a Request for Arbitration, dated 7 May 2008, which Itera and IGVN as Claimants had submitted against Georgia as Respondent on the basis of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (hereinafter the "*Washington Convention*").

28. In the Request for Arbitration, the Claimants alleged that the Respondent had breached its obligations under the US-Georgia BIT and the Netherlands-Georgia BIT in respect of Itera's investment in Azot (hereinafter the "*Azot Dispute*").

29. The Claimants also referred to the dispute with Georgia concerning Sistema (hereinafter the "*Sistema Dispute*") in regard to which arbitration proceedings were pending before ICAC. The Claimants stated, *expressis verbis*, that they "do not advance claims based upon the Sistema Treaty Violations in this Request, while fully reserving their rights to introduce these additional violations into the present proceedings, should their losses not be fully compensated as a result of the ICAC proceedings." (§ 53 of the Request for Arbitration, emphasis added)

30. By letter of 11 December 2008, the parties were notified by ICSID that an Arbitral Tribunal composed of Justice Hans Danelius, Professor Francisco Orrego Vicuña and Professor Brigitte Stern was deemed to have been constituted and the proceedings to have. The parties were also notified that Ms. Natalí Sequeira, Counsel, ICSID, would serve as Secretary of the Tribunal.

31. The First Session of the Tribunal and the parties was held by conference call on 26 January 2009. During the Session, the Tribunal and the parties discussed a number of procedural matters, including the schedule for the written pleadings. In regard to the

Sistema Dispute, the minutes of the Session contain the following statements by the parties:

“Claimants’ position

Claimants have requested Respondent’s agreement to the consolidation of this proceeding with an ongoing ICAC proceeding in Moscow. Although the claims brought in the ICAC proceeding are factually and legally distinct from those presented here, for the reasons mentioned in the Request for Arbitration, consolidation of the two proceedings would serve the interests of efficiency and economy. Consolidation would be particularly sensible considering that: (i) Georgia has taken the position that ICAC is an improper forum for the resolution of state disputes; and (ii) Georgia has denounced in advance any arbitration award that might be rendered in the ICAC proceedings.

Considering Georgia’s categorical refusal to combine the proceedings (see below), the Claimants reserve the right to present the Sistema Treaty Claims before this Tribunal (as already reserved in their Notices of Dispute and Request for Arbitration) in accordance with Rule 40.

Respondent’s position:

Respondent does not consent to the proposed inclusion in this case of the claims currently before the ICAC.

There is no basis to assume that the ICAC claims, which have not been submitted to or registered by the Centre, would satisfy the jurisdictional requirements of Article 25 of the ICSID Convention.

Consolidation would in any event be unwarranted because:

(i) The ICAC claims are, as Claimants have acknowledged, factually and legally distinct from the claims in this ICSID arbitration. The ICAC claims are contractual claims, not even allegedly treaty claims, and concern a contract other than the contract(s) as issue in this ICSID arbitration.

(ii) The language of the two arbitrations is different (the language of the ICAC arbitration is Russian) and consolidation does not justify the cost of translating hundreds of pages of documents from Russian into English.

(iii) The applicable law is different, as Russian law governs the substance and procedure of the ICAC arbitration.

(iv) The final hearing of the ICAC arbitration is scheduled for May 2009 and consolidation would considerably delay resolution of the ICAC claims, drastically increasing costs.

(v) Contrary to Claimants’ implication in its consolidation request, Respondent’s objections to jurisdiction in the ICAC claim do not suggest, explicitly or implicitly, that those claims be instead referred to the Centre.” (Emphasis added)

32. In accordance with the agreed schedule, the Claimants filed their Memorial on 15 April 2009. In this Memorial, they alleged violations of the BIT in regard to both Azot and Sistema. They argued that the Sistema claims were “ancillary” or “additional” claims arising out of the same subject-matter as the Azot claims and that the Tribunal was therefore competent to examine them on the basis of Article 46 of the Washington Convention and Rule 40 of the Arbitration Rules of ICSID.

33. On 4 May 2009, the Respondent raised a number of objections to the Arbitral Tribunal's jurisdiction. In regard to the Sistema claims, the Respondent argued that they were not ancillary claims within the meaning of Article 46 of the Washington Convention and Rule 40 of the ICSID Arbitration Rules, as they did not arise directly out of the subject-matter of the dispute, and that the Tribunal therefore had no competence to deal with them. Other objections related to a "fork-in-the-road" provision in the US-Georgia BIT, to the doctrine of *lis pendens* and to IGV's lack of standing under either the US-Georgia or the Netherlands-Georgia BIT.

34. The Respondent also requested that the Tribunal suspend the proceedings on the merits and order "bifurcation", *i.e.* a separate jurisdictional phase to consider the jurisdictional and admissibility objections raised by the Respondent.

35. On 15 May 2009, the Claimants asked that the Arbitral Tribunal deny the request for "bifurcation". Further submissions on this issue were made on 22 May 2009 by the Respondent and on 27 May 2009 by the Claimants.

36. On 22 June 2009, the Arbitral Tribunal informed the parties that it had decided to grant the Respondent's request for "bifurcation" but only in regard to the question of whether the Sistema claims could be accepted as ancillary claims according to Article 46 of the Washington Convention and Rule 40 of the Arbitration Rules. On this issue, the parties were given the opportunity to make simultaneous further written submissions not later than 31 August 2009 and to present oral arguments before the Tribunal on 15 October 2009.

37. Both parties submitted Memorials on the said issue on 31 August 2009. A hearing was held at the seat of ICSID in Washington, D.C. on 15 October 2009. The Claimants were represented at the hearing by MM. Nigel Rawding, Noah Rubins and Craig Chiasson, of the law firm Freshfield Bruckhaus Deringer, and the Respondent by MM. Paul Friedland, Charles Nairac, Michael Ottolenghi and Ms. Kirsten Odynski, of the law firm White & Case LLP, and Mr. Lasha Arveladze, Ministry of Justice of Georgia.

### **III. RELEVANT LAW**

38. The present arbitration is based on the US-Georgia BIT and the Netherlands-Georgia BIT.

39. Under the US-Georgia BIT, each Contracting Party guarantees national treatment, most-favoured-nation treatment and fair and equitable treatment to investors of the other Contracting Party (Article II). It lays down standards which must be observed in the case of expropriation or nationalization by one Contracting Party of the investments of investors of the other Contracting Party (Article III). It gives the investor a right to ICSID or other arbitration in case of an investment dispute with the State of investment (Article IX).

40. Similarly, the Georgia-Netherlands BIT guarantees fair and equitable treatment, national treatment and most-favoured-nation treatment of investments (Article 3) and



regulates the conditions under which one Contracting Party may deprive nationals of the other Contracting Party of their investments (Article 6). It also allows investment disputes covered by the BIT to be referred to ICSID for arbitration (Article 9).

41. Article 46 of the Washington Convention provides:

“Except as the parties otherwise agree, the Tribunal shall, if requested by a party, determine any incidental or additional claims or counterclaims arising directly out of the subject-matter of the dispute provided that they are within the scope of the consent of the parties and are otherwise within the jurisdiction of the Centre.”

42. Linked to this Article is Rule 40 of the ICSID Arbitration Rules which reads as follows:

**“Rule 40  
Ancillary Claims**

(1) Except as the parties otherwise agree, a party may present an incidental or additional claim or counter-claim arising directly out of the subject-matter of the dispute, provided that such ancillary claim is within the scope of the consent of the parties and is otherwise within the jurisdiction of the Centre.

(2) An incidental or additional claim shall be presented not later than in the reply and a counter-claim no later than in the counter-memorial, unless the Tribunal, upon justification by the party presenting the ancillary claim and upon considering any objection of the other party, authorizes the presentation of the claim at a later stage in the proceeding.

(3) The Tribunal shall fix a time limit within which the party against which an ancillary claim is presented may file its observations thereon.”

43. The Explanatory Notes prepared by the ICSID Secretariat as guidelines to the Arbitration Rules (in effect as of January 1, 1968), provide that for Arbitration Rule 40 the test to satisfy the condition that claims must arise “directly” out of “the subject-matter of the dispute” is “whether the factual connection between the original and the ancillary claim is so close as to require the adjudication of the latter in order to achieve the final settlement of the dispute, the object being to dispose of all the grounds of dispute arising out of the same subject matter”.

#### **IV. THE PARTIES’ CLAIMS**

44. The Respondent requests that the Arbitral Tribunal rule that the purportedly ancillary claims introduced by the Claimants in their Memorial are inadmissible in these proceedings.

45. The Claimants request that the Tribunal:

(a) deny the Respondent’s preliminary objection to the admissibility of the claims relating to the Sistema Treaty Violations;

(b) order the Respondent to pay all of the costs and expenses incurred by the Claimants in relation to the preliminary objection; and

(c) award such other relief as the Tribunal considers appropriate.

## **V. SUMMARY OF THE PARTIES' SUBMISSIONS**

46. The parties' submissions may be summarized as follows:

### **A. The Claimants:**

#### ***(a) Background***

47. The Claimants' claims relate to various investments connected with the restructuring of significant gas debts owed by Georgian state-owned entities to Itera. The claims arose as a result of the actions subsequently taken by Georgia that rendered the Claimants' investments valueless.

48. Both the Azot rehabilitation project and the restructuring of debts through the governmental payment agent Sistema had their genesis in the same activity: the Claimants' pioneering work supplying energy in a newly-independent Georgia. Beginning in 1996, the Claimants supplied gas to state-owned companies and government entities, which accumulated significant debts towards Itera over the years that followed. Itera's negotiations with Georgia resulted in a Debt Restructuring Transaction which formed the foundation for the Claimants' claims in both Azot and Sistema.

49. Thus, the Azot deal was not a self-standing transaction, but was part of the restructuring of Georgia's gas debts. The Sistema Agreements were concluded for precisely the same purpose. Georgia undertook to allocate funds to various state-owned entities, funds earmarked in advance for the repayment of gas debts to Itera, another portion of which was to be repaid through Sistema. The Rehabilitation Decree of 4 October 2003 recorded that investment in Azot was based upon the Debt Restructuring Agreement, which also underlay the Sistema payment arrangement, and it was understood that the proceeds that Itera was to receive from Sistema would be used to help finance Azot's rehabilitation programme.

50. Moreover, Georgia's conduct in relation to Azot was co-ordinated and intertwined with its conduct in relation to Sistema. In fact, Georgia took steps to nullify the entire Debt Restructuring Transaction, including both the privatization of Azot and the guaranteed repayment of debt through Sistema.

#### ***(b) "Ancillary claims"***

51. Georgia has been fully aware of the factual and legal bases of all of the Claimants' claims since at least 18 April 2008, when it was notified of the existence of the present dispute. The Request for Arbitration, submitted to ICSID on 7 May 2008, described the

factual and legal bases for these claims in further detail. In their notification letter and in the Request for Arbitration, the Claimants specifically reserved their rights to seek remedies for the Sistema Treaty Violations in the present proceedings.

52. First, the Claimants' claims form part of a single dispute that was properly brought directly before this Tribunal, depriving Georgia's objection of any basis and eliminating any need to assess whether the Sistema Treaty claims are "ancillary" within the meaning of the Washington Convention and the ICSID Arbitration Rules. Secondly, the Sistema claims also fall within the definition of "ancillary claims" in Article 46 of the Convention and Rule 40 of the Rules.

53. Article 36(2) of the Washington Convention provides that "[t]he request [for arbitration] shall contain information concerning the issues in dispute ...." On the basis of such information, the Secretary-General is to decide whether the request for arbitration is suitable for registration at ICSID. Similarly, Rule 2(1)(e) of the ICSID Institution Rules provides that the request for arbitration shall contain information concerning the issues in dispute, indicating that there is, between the parties, a legal dispute arising directly out of an investment. Itera's Request for Arbitration exceeded in several ways the requirements of Article 36(2) and Institution Rule 2 with respect to the Sistema claims. Thus, Itera fulfilled the requirements of Article 36 and Institution Rule 2 for the presentation of a claim, providing the requisite "information concerning the issues in dispute" in relation to both the Azot and the Sistema elements of the present dispute.

54. By including the Sistema claims in the Memorial, the Claimants did not expand the dispute beyond the elements already before the Tribunal. All of the issues covered in the Memorial had been adequately described in the Request for Arbitration, and are thus properly before the Tribunal.

55. Article 46 of the Convention and Rule 40 of the Arbitration Rules provide mechanisms by which "ancillary claims" may, at the request of a party, be included within the scope of a dispute before a tribunal. In practice, "ancillary claims" are admitted to pending ICSID proceedings in circumstances where (a) they are connected to existing claims, such that it would be procedurally efficient and consistent with the objective of achieving a final resolution of the parties' dispute to adjudicate all claims together; and (b) doing so would not cause undue prejudice to the other party. Arbitral tribunals have adopted a flexible and pragmatic approach to the introduction of ancillary claims, joining claims that presented far more tenuous connections and were raised at a far later stage in the proceedings than the claims under consideration in the present case.

56. The object and purpose of Article 46 and Rule 40 are settled and uncontroversial: to avoid unnecessarily duplicative proceedings, and to facilitate the settlement of the parties' entire dispute, where subsequently filed claims can reasonably be heard simultaneously with existing claims.

57. Accordingly, the presumption must be in favour of consolidating subsequent claims with existing claims, provided that to do so would not cause undue prejudice to the opposing party. The drafters of Rule 40 provided safeguards aimed at ensuring that the

party against whom ancillary claims are directed should not be taken by surprise. These safeguards include the requirement that an “ancillary claim” arise “directly out of the subject-matter of the dispute,” and that time-limits be respected, *i.e.*, no addition of claims after the second round of pleadings. The Sistema claims satisfy both of these pre-requisites.

58. As the various claims currently before the Tribunal are inextricably linked, it would be procedurally inefficient to separate them. A separation would lead to parallel or consecutive proceedings and/or give rise to the avoidable risk of conflicting outcomes. Moreover, the Respondent will suffer no prejudice if the Sistema Treaty claims are adjudicated as part of these proceedings.

59. In addition to the time and resources spent to constitute a second tribunal, this would necessarily entail the preparation and submission of argument and evidence with respect to the same facts and law as have already been presented here. Ultimately, the second tribunal would hear much of the same facts and consider the same evidence, in part given by the same witnesses, as would this Tribunal.

60. Moreover, certain of Georgia’s remaining objections to admissibility and jurisdiction purportedly apply to both Azot and Sistema, and therefore will have to be heard by two tribunals if the current objection is upheld. For example, Georgia argues that IGNV should be dismissed as a claimant with respect to all claims, because its investment was indirect and allegedly not subject to protection under the Netherlands-Georgia BIT.

61. ICSID tribunals have consistently declined to require that claimants make a substantial evidentiary showing at a preliminary stage with respect to the admissibility of their claims. The accepted standard in this regard is *prima facie* evidence that the facts as alleged by the Claimants in this case, if established, are capable of coming within those provisions of the BIT which have been invoked.

62. As is the case with any objection to admissibility, Georgia bears the burden of proof. It must therefore establish to the satisfaction of the Tribunal by competent evidence the elements of its “ancillary claims” objection under Article 46 and Rule 40. However, even setting aside *arguendo* Georgia’s burden of proof, the Claimants have amply demonstrated that the Sistema and Azot Disputes are inextricably linked parts of a single overarching transaction, such that the Sistema claims are clearly ancillary to the Azot claims.

## **B. The Respondent:**

### ***(a) Background***

63. The Debt Restructuring Agreement addressed the restructuring of the debts to Itera of various Georgian public sector organizations and state-owned companies, not including Azot.

64. On the one hand, Itera contacted Sistema to arrange for the repayment of part of the debts covered in the Debt Restructuring Agreement and submitted the Draft Assignment Contract to Sistema and the Draft Surety Agreement to the Ministry of Energy (jointly the “*Draft Sistema Agreements*”). The Draft Sistema Agreements did not mention Azot and did not include any debts of Azot to Itera or its subsidiary Gruzgas.

65. On the other hand, at the same time as Georgia and Itera were negotiating the Draft Sistema Agreements to repay one portion of the debts covered in the Debt Restructuring Agreement, Georgia was negotiating the conditional privatization of Azot with Itera. Azot had been experiencing serious financial difficulties, and a Rehabilitation Plan for the company had been approved in bankruptcy proceedings. By concluding the Sale-Purchase Agreement, Azot undertook to carry out a Business Plan which included the Rehabilitation Plan, but no mention was made of any intended use by Itera of funds from or through Sistema to fulfil its obligations under this Business Plan. It was never understood that Itera would use the proceeds from the debt payments under the Debt Restructuring Agreement to help finance Azot’s revitalization program, in accordance with the Business Plan, or that the funds that Georgia committed to provide in performance of the Sale-Purchase Agreement and the Surety Agreement were to be used to advance the acquisition and rehabilitation of Azot. It is also a fact that neither the Debt Restructuring Agreement nor the other Sistema-related documents refer to Azot.

**(b) “Ancillary claims”**

66. In order to constitute an “additional” or “ancillary” claim admissible under Article 46 of the ICSID Convention, the Sistema Dispute must arise directly out of the subject-matter of the Azot Dispute already submitted to the Arbitral Tribunal. According to Note B to ICSID Arbitration Rule 40, the test to satisfy this ancillary jurisdictional condition is whether the factual connection between the original and the new claim is so close as to require the adjudication of the latter in order to achieve the final settlement of the dispute, the object being to dispose of all the grounds of dispute arising out of the same subject-matter. The Claimants do not satisfy this test. Resolution of the Azot Dispute does not require adjudication of the Sistema Dispute.

67. In the Azot Dispute, the Claimants allege that the Respondent interfered with the Claimants’ investment in Azot by (i) failing to honour its commitments under the agreement governing the conditional privatization of Azot, (ii) pursuing an improper and unfair bankruptcy process directed at Azot, and (iii) wrongfully “re-privatizing” Azot. Resolution of the Azot Dispute will require the Tribunal to address a set of agreements for privatization and rehabilitation of the Azot plant and a series of administrative actions taken by the Respondent in relation to Azot. None of these allegations relates to Sistema. The Sistema Dispute, by contrast, concerns a separate series of agreements involving Sistema for repayment through Sistema of energy debts of Georgian public sector organizations and state-owned companies to Itera.

68. The Claimants have by their litigation conduct and choices confirmed that the resolution of the Azot Dispute is independent of the Sistema Dispute and vice versa. The Claimants submitted to arbitration before ICAC in Moscow, claims that are factually

indistinguishable from those that comprise the Sistema Dispute in this case. The Claimants then submitted the Azot Dispute to ICSID arbitration, without seeking to include the Sistema Dispute therein. The Claimants knew of the Azot Dispute when they started the ICAC arbitration in January 2006, and they knew of the Sistema Dispute when they commenced the present arbitration, but judged it unnecessary or not useful to include the Sistema Dispute in this case. They have now changed their mind about their tactical choices, but this change of mind does not change the underlying facts, which permitted them to pursue each set of claims separately.

69. As the Claimants have initiated the ICAC arbitration and pursued it for three years, they can suffer no prejudice from the dismissal of the Sistema Dispute from the present proceedings. Admitting the Sistema Dispute, by contrast, would be prejudicial to the Respondent, which has expended considerable time and resources in defending the Sistema Dispute in the ICAC arbitration for the past three years, and which now would be faced by vastly increased costs to re-litigate those claims in this case. Were the Sistema Dispute to be accepted in this case, the Tribunal would reward the Claimants' forum shopping and create the risk of conflicting decisions on virtually identical sets of Sistema-related claims.

70. To support their effort to switch fora, the Claimants are compelled to establish a link between the two disputes. The Debt Restructuring Agreement, which addresses a series of Georgia's energy sector debts and calls for payments through a financial agent which would later be Sistema, does not cover the Azot-related transactions, or even mention Azot.

71. The Claimants have evoked a "Debt Restructuring Transaction" that supposedly covered both the Azot and Sistema transactions, and they have also alleged that "it was understood" that payments made pursuant to any and all agreements associated with such "Transaction" would be used by Itera to rehabilitate the Azot plant. However, there is no basis to find either that a "Debt Restructuring Transaction" ever existed or that there was any "understanding" linking Azot thereto.

72. The Debt Restructuring Agreement created a framework for the repayment of USD46,406,352.30 to Itera according to a seven-year repayment schedule. It does not discuss Azot at all, and its implementation neither requires, nor is served by, any of the agreements subsequently entered into in relation to Azot.

73. The Azot agreements, and the Azot Dispute, lie elsewhere. In connection with the conditional privatization of Azot, which is at the heart of the Azot Dispute, Itera was keen to use outstanding Azot tax debts to operate a set-off with some of the debts owed to Itera by Georgian public sector organizations and state-owned companies. The parties therefore carved out some of the debts listed in the Debt Restructuring Agreement, and provided for a set-off mechanism instead of repayment pursuant to the Debt Restructuring Agreement. The Azot Dispute concerns the monies covered by the Azot Debt Set-Off Agreement, which are different from those addressed in the Sistema agreements, and not any other sum under the Debt Restructuring Agreement.

74. There is thus no meaningful factual or legal connection between the Sistema Dispute and the Azot Dispute, let alone a connection that establishes that the Sistema Dispute arises directly out of the subject-matter of the Azot Dispute or a factual connection between the original and the new claim so close as to require the adjudication of the latter in order to achieve the final settlement of the dispute (cf. Note B to ICSID Arbitration Rule 40).

75. In any case, the Claimants have the burden of proof and must establish that their new claims relating to the Sistema Dispute arise directly out of the subject-matter of the original dispute. They cannot meet their burden of proof because the Azot and Sistema Disputes are based on different facts and debts, and allege different wrongs against Georgia, and the resolution of the Azot Dispute does not therefore require the Tribunal to resolve the Sistema Dispute. Admitting the Sistema claims as ancillary claims would directly undercut the rationale behind Article 46 and Rule 40 as it would be counter to judicial economy and potentially lead to conflicting outcomes between these proceedings and the ICAC arbitration. Admitting the Sistema claims would also be unfair to the Respondent, which has already gone through three years of defending factually indistinguishable claims in the ICAC arbitration.

76. In deciding whether the Claimants' new claims are admissible in this arbitration, the Tribunal need not consider any of the many issues that will be presented at the merits stage. No questions of performance arise. No questions of quantum arise. A decision by the Tribunal that the Claimants' new claims are inadmissible in this separate phase of proceedings would create very substantial cost savings for both parties in this arbitration.

77. Finally, and independently of the separateness of the Azot and Sistema Disputes, there is a defect in the Claimants' consent to the Tribunal's jurisdiction over the Sistema Dispute.

78. Resolution of the Sistema dispute will require the Tribunal to consider the Draft Assignment Contract and the Draft Surety Agreement. Resolution of the Azot Dispute will require the Tribunal to consider the Sale-Purchase Agreement and the Business Plan as well as the Set-Off Agreement and Decree No. 503. The Tribunal will not need to address the Draft Assignment Contract and the Draft Surety Agreement to resolve the Azot Dispute, and the Sistema Dispute does not therefore arise "directly out of the subject-matter" of the Azot Dispute.

79. In their letter instituting these ICSID proceedings, the Claimants "formally consent[ed] to submit their investment dispute with Georgia concerning the Azot Treaty Violations to international arbitration under the [ICSID Convention]". The Claimants also reserved their "rights" to introduce the Sistema Dispute at a later time "should [Itera's] losses not be fully compensated as a result of the ICAC proceedings". In their Request for Arbitration, the Claimants again excluded the Sistema Dispute from these proceedings, noting that they did "not advance claims based upon the Sistema Treaty Violations". Such exclusion places the Sistema Dispute outside the "scope of consent of the parties" under Article 46 of the ICSID Convention and ICSID Arbitration Rule 40. The Claimants' previous lack of consent to the submission of the Sistema Dispute to

ICSID therefore means that the Sistema Dispute is inadmissible in these proceedings as it was not “within the jurisdiction of the Centre” at the time the Azot Dispute was submitted. Nor can the Claimants purport even to exercise the “right” reserved in their letter exercising ICSID proceedings to introduce the Sistema Dispute in the Memorial, as such reservation of rights was based on a condition that has not occurred, *i.e.* the conclusion of the ICAC proceedings.

80. The dismissal of the Sistema Dispute in these proceedings would entail considerable savings, including:

- (a) saved costs associated with the briefing and arguing of issues relevant only to the Sistema Dispute, including the costs associated with additional hearing time;
- (b) saved costs associated with the translation of Russian and Georgian language documents relevant solely to the Sistema Dispute; such documents are not the same as the documents that bear upon the Azot Dispute;
- (c) saved costs associated with the preparation of an expert report on relevant issues of Russian law; the Azot Dispute, by contrast, involves no issues of Russian law; and
- (d) saved costs associated with the issue of the quantum of compensation due for Georgia’s alleged breaches of the Surety Agreement.

81. If, on the other hand, the Tribunal decides to admit the Sistema Dispute into these proceedings, the parties may face conflicting decisions on the Sistema Dispute. Conflicting decisions are usually avoided, and judicial efficiency is usually served, by consolidating claims into one set of proceedings, but in this case the Claimants’ attempt to introduce into these proceedings the Sistema Dispute that was already the subject of the ICAC arbitration has created the opposite situation. Only the Tribunal’s dismissal of the Sistema Dispute from these proceedings could avoid potentially conflicting decisions and serve interests of judicial efficiency and comity. Admitting the Sistema Dispute would reward the Claimants’ tactical forum shopping and set a dangerous precedent in investment arbitration.

## **V. THE TRIBUNAL’S REASONING**

82. On 22 June 2009, the Arbitral Tribunal decided to grant the Respondent’s request for “bifurcation” but only in regard to the question of whether the claims in the Sistema Dispute can be accepted as ancillary claims in the present case according to Article 46 of the Washington Convention and Rule 40 of the ICSID Arbitration Rules.

83. In their subsequent submissions, the Claimants argued, as a first line of defence, that it would not be necessary for the Arbitral Tribunal to respond to this question, since, in their view, the Sistema and Azot claims form part of one single dispute which in its entirety was properly brought before the Tribunal in the Request for Arbitration. The Claimants contended that the Sistema Dispute had been sufficiently described in the Request for Arbitration and argued that, by including claims regarding Sistema in their



Memorial, they had not expanded the case beyond what had already been submitted to the Tribunal. The Claimants argued that, having regard to these circumstances, the Respondent's objection based on Article 46 of the Washington Convention and Rule 40 of the ICSID Arbitration Rules was moot and should be denied.

84. The Arbitral Tribunal is not convinced by the Claimants' argument on this point. An arbitration is essentially delimited by the parties' claims and not by the contents of their submissions in so far as they are unrelated to any specific claim for relief.

85. In this case, the Claimants, in their Request for Arbitration, described their disputes with Georgia regarding Azot as well as Sistema. They presented claims against Georgia based on allegations of Treaty violations in respect of Azot but declared that they did not, for the time being, make any claims on the basis of the facts relating to Sistema, while fully reserving their rights to do so in the future.

86. The Arbitral Tribunal thus finds it clear that in the Request for Arbitration the only dispute submitted for arbitration was the Azot Dispute. The fact that the Claimants also described the Sistema Dispute and even reserved the right to present claims relating to that dispute at a later stage does not mean that the Sistema Dispute was already part of the case submitted to ICSID for arbitration.

87. It follows that the Claimants' argument that the Sistema Dispute was already part of the case and that no question of adding an ancillary claim arises must be rejected.

88. The Tribunal is therefore called upon to examine whether the Claimants were entitled, according to Article 46 of the Washington Convention and Rule 40 of the ICSID Arbitration Rules, to extend the scope of the arbitration in their Memorial by including the Sistema claims as ancillary claims.

89. Ancillary claims under Article 46 of the Washington Convention and Rule 40 of the ICSID Rules are incidental or additional claims arising directly out of the subject-matter of the dispute. The crucial question is therefore whether or not the Sistema claims can be considered to arise directly out of the subject-matter of the Azot Dispute, the latter being the only dispute submitted for arbitration in the Request for Arbitration.

90. The Arbitral Tribunal recognizes that there is a link between the Azot and Sistema Disputes in so far as they had a common purpose of ensuring payment of debts to Itera. To some extent this common background appears from the Debt Restructuring Agreement which laid down a general pattern of repayment of Georgian state debts to Itera.

91. The total debt dealt with in the Debt Restructuring Agreement was US\$ 46,406,352.30. Out of this amount, the Sistema Agreements provided for the repayment of US\$ 13,564,946.29, and the Azot Agreements were intended to result in repayment through a set-off transaction of GEL22,111,941 (the equivalent of approximately US\$ 10.2 million). This amount represented a tax debt of Azot which Itera was supposed to pay but would not be claimed by the Ministry of Finance of Georgia in exchange for an

equivalent amount being deducted from the amounts owed to Itera by various public entities mentioned in the Debt Restructuring Agreement.

92. The method of repayment envisaged in the Debt Restructuring Agreement was that Itera would assign claims to a financial agent selected by the Energy Ministry which would then repay to Itera the amount of the claims in quarterly instalments within a period of seven years starting as of 2003. This method was implemented when the Ministry of Fuel and Energy designated Sistema as financial agent and the Assignment Contract was concluded providing for the assignment by Itera of claims to Sistema and for corresponding subsequent payments by Sistema to Itera over a period of seven years in quarterly instalments.

93. However, a different method of repayment of debts to Itera was chosen in the Azot Agreements of 20 March 2003 which provided for repayment to Itera by way of a set-off arrangement in connection with Itera's acquisition of Azot at a low price. In the Azot Agreements, there was no question of repayments by a financial agent designated by Georgia, nor were the repayments to take place periodically over a certain time period. The link between the Debt Restructuring Agreement and the Azot Agreements was therefore weak, and the Azot Agreements can only in an indirect manner, be considered an implementation of the Debt Restructuring Agreement.

94. It may also be noted that, while the Debt Restructuring Agreement and the Sistema Agreements involved the Ministry of Energy and its financial agent Sistema and concerned direct repayment of debts, the Azot Agreements were concluded with the Ministry of State Property Administration and the Ministry of Finance and dealt essentially with the privatization of Azot and the payment of Azot's fiscal debts, although, by means of a set-off transaction, they also served the purpose of providing Itera with satisfaction for some of its claims..

95. The Tribunal notes that as a part of its acquisition of 90% of the shares in Azot, Itera undertook to carry out a Business Plan which included a plan for the rehabilitation of the company approved by the competent court in bankruptcy proceedings. Another element in the transaction was that the Ministry of Finance would guarantee that a bill was submitted to Parliament about funds being made available for repayment of debts to Itera which in its turn would pay Azot's fiscal debts to the Ministry of Finance. The Respondent argues that Itera failed to fulfil its obligations under the Business Plan, while Itera considers that Georgia failed to make the required payments to Itera and also took action which eventually caused the bankruptcy of Azot and the forced sale of its assets.

96. The Tribunal thus observes that the Azot Dispute essentially centres around questions as to whether Itera and/or Georgia carried out their respective undertakings to ensure the continued existence of Azot and what were the decisive factors which ultimately led to Azot's bankruptcy and to Itera's loss of its investment.

97. The Sistema Dispute, on the other hand, essentially concerns questions of whether the Debt Restructuring Agreement and the Sistema Agreements, in particular the Surety

Agreement, had been validly concluded and, if so, why there was no repayment to Itera of US\$ 13,564,946.29 under the Sistema Agreements.

98. The Arbitral Tribunal notes that the facts of the present case differ significantly from those of other ICSID cases<sup>2</sup> in which new claims were accepted as ancillary claims. In those cases, the new claims related to the same investments as the original claims

99. In *CMS*, the tribunal pointed out that the important factor was the subject-matter of the dispute and found that, in that case, the subject-matter was the alleged loss by CMS of its investment in a company. The subsequent claims submitted by the Claimants as ancillary, were accepted by the tribunal as ancillary, since the acts of the Argentine Government initially complained of and the new claims resulted in the same loss.. In *Enron*, the Claimants presented a request concerning the adoption by the Argentine Government of certain additional measures which were alleged to affect the same investment as was the subject of the initial request for arbitration. The tribunal accepted that this was an ancillary claim without any specification of the criteria that would be decisive for such acceptance, but it may be assumed that the tribunal relied on the same analysis as in *CMS*, finding that the claims related to the same investment and the same loss. The circumstances of the present case are different in so far as, in the Azot claims, the loss complained of is the loss of the Azot company by expropriation, whereas, in regard to the Sistema claims, the loss results from the alleged failure of Sistema to reimburse debts to Itera. While the investor is the same, it entered in two different types of relationship with Georgia, which, in the view of the Tribunal, cannot be analyzed as a single investment.

100. In support of their contention that the Sistema claims are ancillary to the Azot claims, the Claimants have also relied on an argument of efficiency, arguing that it would be more efficient for one and the same tribunal to deal with all Itera's claims against Georgia. However, under Article 46 of the Washington Convention and Rule 40 of the ICSID Rules, efficiency considerations are not in themselves decisive for whether or not a new claim shall be accepted as an ancillary claim, but the subject-matter must be the same, which means that the link between the claims must be so strong that the examination of one claim cannot be carried out adequately without the other claim being adjudicated at the same time. No such situation exists in the present case. The Tribunal notes in this respect that the Claimants themselves considered for a long time that the two claims could be dealt with separately and limited their Request for Arbitration to the Azot claims. It is not denied that efficiency may in some circumstances be a result of, a claim being accepted as ancillary. However, it is at least doubtful whether acceptance of the Sistema claims as ancillary would promote efficiency, as it would involve a new examination of matters that have already been discussed for a long time before another arbitral tribunal.

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<sup>2</sup> *CMS Gas Transmission Co. v. the Argentine Republic* (ICSID Case No. ARB/01/8), Decision on Objections to Jurisdiction, 17 July 2003, *LG&E Energy Corp., LG&E Capital Corp. and LG&E International, Inc. v. the Argentine Republic* (ICSID Case No. ARB/02/1), Decision on Objections to Jurisdiction, 30 April 2004, *Enron Corporation and Ponderosa Assets L.P. v. the Argentine Republic* (ICSID Case No. ARB/01/3), Decision on Jurisdiction (Ancillary Claim), 2 August 2004.

101. The Tribunal thus considers that, despite a certain common background of the Azot and Sistema Disputes, the Sistema Dispute cannot be considered to arise directly out of the Azot Dispute and the subject-matter cannot be considered to be the same. It follows that the conditions laid down in Article 46 of the Washington Convention and Rule 40 of the ICSID Rules are not satisfied and that the Sistema claims cannot be accepted as ancillary to the Azot claims.

102. In regard to the Claimants' claim for costs, the Arbitral Tribunal considers that this claim relates to the general issue of costs which will be examined at a later stage of the proceedings.

## **DECISION**

103. The Arbitral Tribunal decides that the Sistema claims were not part of the dispute brought before the Tribunal in the Request for Arbitration and are not ancillary claims according to Article 46 of the Washington Convention and Rule 40 of the ICSID Arbitration Rules.

104. Professor Orrego Vicuña's dissenting opinion is attached to this Decision.

[*SIGNED*]

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Professor Francisco Orrego Vicuña  
Member of the Tribunal  
Date: November 30, 2009  
**Subject to the attached dissenting opinion**

[*SIGNED*]

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Professor Brigitte Stern  
Member of the Tribunal  
Date: November 20, 2009

[*SIGNED*]

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Justice Hans Danelius  
President of the Tribunal  
Date: December 3, 2009