Russia’s Continued Consolidation Of Its Oil And Gas Sector

Early this month, President Putin publicly threatened one of the biggest deals in Russia’s ongoing campaign to assert its control over the country’s energy sector. The project is for the development of the Kovykta gas field, one of the country’s largest and most controversial energy deals over the past few years. The Kremlin’s consolidation of control over the Russian oil and gas industries has had as a consistent feature an attack on projects based on allegations of negative environmental consequences of the project. The nationalization of Yukos was premised on claims that Yukos failed to pay the requisite regional development taxes on behalf of its alleged export trading companies.

The Kremlin’s consolidation of control over the Russian oil and gas industries has had as a consistent feature an attack on projects based on alleged regulatory violations and lack of local developmental impact. The nationalization of Shell’s investment in the Sakhalin II project in December 2006 was based on claims of negative environmental consequences of the project. The nationalization of Yukos was premised on claims that Yukos failed to pay the requisite regional development taxes on behalf of its alleged export trading companies.

Commentators have pointed out that, for President Putin, there is no conflict between the consolidation of the Russian energy sector under state control and its use to further foreign policy goals. President Putin’s 1999 doctoral thesis described the consolidation of Russia’s oil and gas wealth as serving, at least partially, foreign policy goals as to lead to “the country’s reemergence as an important international actor.” During both of the past two winters, Russia has halted the supply of gas, first to the Ukraine in January 2006 and then to Belarus in December of the same year.

In the current climate, investors should be aware of possible international legal options. For example, Russia is a signatory to at least 30 Bilateral Investment Treaties with countries including the United Kingdom, the Netherlands, France, Germany, and Italy. Russia has signed but has yet to ratify a bilateral agreement with the United States. Russia is also a signatory to, but has not ratified. Although President Putin has stated that he will not ratify the Energy Charter Treaty in its current form, to which more than 45 countries are parties, Russia’s consent to arbitration under the ECT has been asserted by investors alleging wrongful expropriation in connection with the Yukos nationalization. There has not yet been a resolution of the issue in these arbitrations.

Milbank Tweed has significant expertise in investor-state dispute resolution in general and arbitration pursuant to the Energy Charter Treaty in particular. We also have extensive Eastern European experience and are industry leaders in energy transactions and restructurings. Our experience may allow us to be of assistance as events in Russia continue to unfold.

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3 See id.
7 See id. at pp. 16-23.