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1. Introduction

On 24 February 2022, Russia launched an armed invasion of Ukraine in violation of international law, which has been widely condemned by the international community.¹ While the war is ongoing and millions of Ukrainians continue to flee their homes and their country, Russia has become subject to a wide range of sanctions imposed by the United States, the European Union, Japan and other countries. In return, Russia has compiled a list of “unfriendly countries”, including Japan, and is beginning to impose sanction countermeasures.²

This newsletter does not aim to focus on the sanctions themselves, which we have analyzed elsewhere,³ but addresses steps and possibilities Japanese investors should be aware of in the current situation. Sanctions, “counter-sanctions”, and decisions not to indirectly finance the Russian aggression against Ukraine are all considerations that many Japanese companies conducting business in Russia now face.

This newsletter first briefly explains the risks that Japanese investors currently encounter in Russia and highlights general considerations and options available for Japanese companies. The second part provides an overview of potential remedies Japanese investors have at their disposal against Russia under the international investment protection mechanism in place between Japan and Russia.

¹ On 16 March 2022, the International Court of Justice granted Ukraine’s request for provisional measures raised under the Genocide Convention against Russia. The Court found with thirteen votes to two that the Russian Federation shall immediately suspend the military operations that it commenced on 24 February 2022 in the territory of Ukraine and, unanimously, that both parties shall refrain from any action which might aggravate or extend the dispute before the Court or make it more difficult to resolve. See for the Court’s summary at <https://www.icj-cij.org/public/files/case-related/182/182-20220316-SUM-01-00-EN.pdf>.

² Mainichi Japan, Russia adds Japan to 'unfriendly' countries, regions list in sanctions countermeasure, 8.3.2022, <https://mainichi.jp/english/articles/20220308/p2a/00m/0na/007000c>.

³ Please see for first observations on the sanctions in the Japanese N&A Newsletter ウクライナ情勢を受けた欧米日の対ロシア制裁の直近動向 Part 1 https://www.nishimura.com/ja/newsletters/europe_220228.html, Part 2 https://www.nishimura.com/ja/newsletters/europe_220304_2.html and Part 3 https://www.nishimura.com/ja/newsletters/europe_220317.html.

Also with focus on sanctions in the energy sector, the Japanese N&A Newsletter エネルギー分野における対ロシア制裁の最新動向 Part 1 https://www.nishimura.com/ja/newsletters/europe_220304.html and Part 2 https://www.nishimura.com/ja/newsletters/europe_220311.html.

2. General Considerations and Options considering the Extraordinary Situation

The sanctions imposed on Russia will severely impact the Russian economy and possibilities for Japanese investors to conduct their business in Russia. Due to the rapidly-evolving situation with respect to additional sanctions and potential secondary sanctions, it is important to stay informed and to react swiftly and diligently to the changing circumstances to avoid running afoul of applicable sanction regimes. Business with or in Russia is complicated by the fact that the imposed sanctions not only target the Russian government, but also entities or persons closely related to it, the Russian military, as well as Russian banks. Japanese companies will therefore in many instances consider cutting business ties with such entities or persons at short notice.

It also needs to be kept in mind that business activities in Russia generally, but in particular those with a connection to Russia's government, are the subject of public scrutiny and discussion. Japanese companies invested in Russia will want to carefully assess and review their business position and structure in the country, not least to avoid becoming complicit in unconscionable human rights abuses, facing a negative impact on their environmental, social, and governance (ESG) efforts, or even indirectly contributing (financially) to Russia's war in Ukraine. Even where this is not the case, the retreat from the Russian market or the discontinuation of operations of countless global heavyweights such as Apple, Visa, Mastercard, Mercedes-Benz, McDonalds, Coca Cola, Netflix, Meta (formerly known as Facebook), Nestlé, General Electric, and Shell, to name just a few, will certainly add pressure on global Japanese businesses to follow suit. We are aware that a considerable number of Japanese companies are currently assessing their options, and some of them have already suspended operations.

When weighing the risk of a withdrawal from the Russian market, Japanese companies must be aware that Russia might take its own countermeasures. In fact, the Russian government has already hinted at plans for the nationalization or expropriation of assets of foreign businesses which end or suspend business in light of the war against Ukraine.⁴ For example, on 14 March 2022, Russia paved the way for domestic airlines to appropriate hundreds of foreign-owned planes worth around USD 10 billion. These planes had been leased by Russian airlines and are now trapped in Russia, after foreign registries suspended their certifications in order to comply with sanctions.⁵ Russia's government has also announced other measures, like restrictions or the end of patent protection for foreign companies,⁶ limitations on cash exports, contemplation of insolvency proceedings or criminal liability for foreign companies leaving Russia, and even suspension of stock trading since the first sanctions were imposed, as well as introducing mandatory sales of currency proceeds.

Given the exodus of foreign companies and investors from Russia, Japanese companies' projects with non-Russian or multiple project partners might disintegrate. Disputes could therefore arise in a variety of situations, involving different stakeholders. A review of the current business position in Russia should also extend to the dispute resolution mechanisms in place, including necessary adjustments. The importance of a robust and impartial dispute resolution mechanism is obvious if one considers the extraordinary situation

⁴ Washington Post, Russia considers nationalizing Western businesses that have closed over Ukraine invasion, 10.3.2022, <https://www.washingtonpost.com/business/2022/03/10/russia-nationalize-foreign-business-ukraine/>.

⁵ Fortune, Russia sets plan to steal \$10 billion worth of foreign planes held in the country, 15.3.2022, <https://fortune.com/2022/03/15/russia-planes-foreign-owned-leasing-putin-confiscate-theft/>.

⁶ Washington Post, Russia says its businesses can steal patents from anyone in 'unfriendly' countries, 9.3.2022, <https://www.washingtonpost.com/business/2022/03/09/russia-allows-patent-theft/>.

which Russia is currently facing. The impartiality of national courts may always be an important concern for Japanese investors abroad, but will be under particular scrutiny in a jurisdiction which is heavily sanctioned, heavily censored, and in the middle of a war. While it remains to be seen what effect the current situation will have on Russia's judiciary, it does not bode well for companies which the Russian government considers not to be acting in its interest.

Japanese companies should therefore review their relevant contracts and assess whether they contain valid arbitration agreements. While companies decide to include arbitration agreements for a variety of reasons in their contracts, it is widely acknowledged that a valid arbitration agreement prevents its signatories from resorting to litigation if the dispute falls within the scope of the arbitration agreement. Arbitration enables companies to have their dispute adjudicated in an impartial, efficient, and usually confidential manner.

In the below we will describe an additional avenue for Japanese investors to enforce their rights in Russia. Japan has concluded a bilateral investment treaty with Russia ("**Japan-Russia BIT**"), specifically with the aim of protecting Japanese investments in Russia and providing the opportunity for Japanese companies to initiate arbitration proceedings against the Russian government if their rights are infringed.

3. Investment Protection and its Enforcement

The Japan-Russia BIT has been in force since 27 May 2000 and allows Japanese investors to raise claims directly against the Russian state if its actions (or actions attributable to it) violate provisions for the protection of covered Japanese investments. The below will explain in what cases such a claim might exist and how it can be enforced. As the existence of a claim will depend on the individual circumstances of each case, the summary can only constitute general guidelines. Each company's situation will have to be assessed individually, considering the facts of the case and the legal provisions applicable to it.

(1) Investment Protection

A Japanese company can only rely on the investment protection provided by the Japan-Russia BIT if it qualifies as an investor, and its Russian business as an investment, under the BIT. Whether this is the case will depend on the specific circumstances. Generally speaking, the Japan-Russia BIT (in Article 1) is not restrictive and adopts a broad definition of investor and investment, covering investments made before the entry into force of the BIT, and a broad category of asset classes.

The two main standards of protection open to Japanese investors under the Japan-Russia BIT are the so-called fair and equitable treatment standard ("**FET**") in Article 3(3) of the BIT and compensation in case of expropriation in Article 5 of the BIT. The FET standard is not defined in the BIT, opening a wide range of applications to a particular case. State actions that are typically considered to constitute a breach of the FET standard are, for example: (a) unreasonable, arbitrary and discriminatory treatment; (b) failure to offer a stable and predictable legal framework; (c) lack of transparency and denial of due process and justice; and (d) frustration of legitimate expectations. The standard of what constitutes a direct or indirect expropriation for which compensation is due is likewise heavily influenced by past decisions of arbitral tribunals and will have to be analyzed on a case-by-case basis. However, it stands to reason that Russia's planned nationalization of foreign companies' assets could be encompassed by Article 5 of the Japan-Russia BIT.⁷

⁷ See also for a comment on Russia's expropriation plans in light of international law by Nishimura & Asahi's [Kojiro Fujii](https://www.nikkei.com/nkd/industry/article/?DisplayType=2&n_m_code=035&ng=DGKKZO59029290S2A310C2EA2000) in Japanese at Nikkei.com, 対口経済封鎖、企業に試練, 12.3.2022, https://www.nikkei.com/nkd/industry/article/?DisplayType=2&n_m_code=035&ng=DGKKZO59029290S2A310C2EA2000.

(2) Enforcement Mechanism

The Japan-Russia BIT not only protects Japanese investments in Russia, but it also contains the option for Japanese investors to initiate arbitral proceedings against Russia (Article 11 of the BIT) if the protections are infringed. Before an investor can initiate an arbitration, it must attempt to settle the dispute “amicably through negotiations” between the investor and Russia, as well as terminate pending national proceedings. If there is no settlement by amicable negotiations, Japanese investors can initiate arbitration under the widely-used UNCITRAL Arbitration Rules or under the ICSID Additional Facility Rules.⁸

Based on our experience, States have been reluctant to make the existence and content of investment arbitrations public. To this end, the prospect of an investment arbitration alone may lead to a favorably-negotiated outcome for the investor, although in the case of Russia under the current situation one should not be too optimistic. Russia has been involved in – and lost – a number of investment arbitrations. While Russia does not always comply with arbitral awards rendered against it, Japanese investors will in principle be able to enforce a potential award rendered against Russia in all 169 signatory states to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (so-called New York Convention).⁹ Since, as a consequence of the recent sanctions against Russia, a substantial amount of Russian assets have been frozen abroad, the chances for Japanese investors to successfully enforce an arbitral award would considerably increase if the freezing orders were still in place by the time the award is rendered.

4. Conclusion

The current situation for Japanese investors in Russia is challenging. Many good reasons speak for ending or suspending business in Russia, in line with a clear trend observed for global companies. On the other hand, Japan’s national security and energy interests as well as geopolitical implications may warrant a more nuanced assessment. Either scenario will require a careful analysis of current business structures and business partners, including the contractual regimes and potential disputes arising in this context.

The Japan-Russia BIT provides additional protection for Japanese investors in case Russia makes good on its threat to nationalize foreign assets of businesses withdrawing from the Russia market. Should you be interested in learning more about this topic, please do not hesitate to contact us and feel free to watch an exclusive [N&A webinar on investment-arbitration \(in Japanese\)](#) for additional information and an introduction to our investment arbitration practice.¹⁰

⁸ Russia has never ratified the ICSID Convention.

⁹ For an instructive and at the same time entertaining account of such an endeavor by a victorious German investor, see Sedelmayer/Weisman, Welcome to Putingrad, The Incredible Story of the Only Man to Collect Money from Vladimir Putin (2017).

¹⁰ N&A Legal Forum Online, Investment Arbitration Webinar Series, at <https://www.nishimura.com/ja/seminars/LFO20210421.html>.

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