

Legal Alert

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QUESTION: WHAT CAN YOU DO WHEN VLADIMIR PUTIN AND HIS RUSSIAN CRONIES DESTROY YOUR BUSINESS?

ANSWER: FORMER YUKOS OIL COMPANY SHAREHOLDERS WERE AWARDED MORE THAN \$50 BILLION AGAINST THE RUSSIAN FEDERATION BY THE PERMANENT COURT OF ARBITRATION IN THE NETHERLANDS!

Government greed and power!

OAQ Yukos Oil Company (“Yukos Oil”) became Russia’s largest oil company after the breakup of the Soviet Union. In early 2003, Yukos was merging with Sibneft, another large Russian oil company. Had the merger been completed, it would have formed the fourth largest oil company in the world. Vladimir Putin and the Russian government wanted the Yukos Oil assets for Rosneft, the Russian state oil company, however. So Yukos Oil was destroyed and Rosneft got the assets! (Final Award of 18 July 2014, *Yukos Universal Limited (Isle of Man) v. The Russian Federation*, Permanent Court of Arbitration.)

What happened?

Unfortunately, the CEO of Yukos, Mikhail Khordokovsky, said the wrong thing, at the wrong time, to the wrong person! “The turning point, . . . was a meeting at the Kremlin between President Putin and the Russian Union of Industrialists and Entrepreneurs on 19 February 2003, . . . at which Mr. Khordokovsky delivered a speech about corruption in Russia.” (Final Award of 18 July 2014). Mr. Putin does not take constructive criticism very well! By early 2003 “Mikhail Khordokovsky’s participation in the social policy and political spheres in Russia, coupled with Yukos’ growing economic power, came to be perceived as a threat by the Russian authorities.” President Vladimir Putin’s former Chief Economic Advisor, Dr. Illarionov stated that a “special unit was set up at the General Prosecutor’s office, comprised of approximately 50 people and working exclusively on fabricating evidence against Mr. Khordokovsky and Yukos.” Mr. Khordokovsky was imprisoned in 2003. (The Russians don’t seem to have a long, drawn-out grand jury process, or for that matter, any due process whatsoever.) Mr. Khordokovsky

was convicted of fraud and tax evasion, and spent more than a decade in Russian prisons.

Taxation as theft.

Mr. Putin and the Russian government also went after Yukos Oil. As all governments know, the most powerful way to punish is taxation. After the candid comments about Russian corruption and the jailing of Mr. Khordokovsky, Russia also started reassessing the tax liability of Yukos Oil. Russia demanded payment of \$24 billion in allegedly unpaid taxes and fines.

Russia ignored offers by Yukos Oil to settle the tax liability and began seizing assets of Yukos Oil. The Tribunal found: “[Russia’s] total failure to engage with any of Yukos’ settlement proposals raises significant doubts... as to whether [Russia’s] true and sole concern in its dealings with Yukos after the tax assessments were issued was the collection of taxes.”

One of the main assets of Yukos Oil was called Yuganskneftegaz (“YNG”). Russia sold YNG at a forced auction on a Sunday afternoon on the outskirts of Moscow. While international banks valued YNG at \$15 to \$18 billion, only one bid was received for \$9.25 billion. The buyer at the auction was a sham entity capitalized with only \$359. Rosneft, the Russian state oil company, acquired the assets three days after the auction.

Eventually in 2006, Russia forced Yukos Oil into bankruptcy and its remaining assets were sold. It went out of business completely in 2007.

In addition to the punitive and confiscatory taxation, Russia made it impossible to run the business of Yukos Oil by frequently raiding its offices and taking its documents. Russia harassed Yukos and its employees and anyone who dealt with it.

How do you get a \$50 billion arbitration award against a rogue government?

Three large former shareholders of Yukos Oil alleged that Russia breached the Energy Charter Treaty (over 50 countries have signed the Energy Charter Treaty). Among many things, the Energy Charter Treaty requires countries to treat foreign investments in a fair and equitable manner without discrimination. The Treaty also prohibits countries from expropriating investments without payment of prompt and adequate compensation. Such expropriation has to be in the public interest, non-discriminatory, and afford due process of law.

The Yukos Oil shareholders elected to pursue their claims against the Russian Federation through international arbitration under the rules of the United Nations Commission on International Trade Law (UNCITRAL). The arbitration was administered by the Permanent Court of Arbitration in the Hague.

The Tribunal concluded that “the primary objective of the Russian Federation was not to collect taxes but rather to bankrupt Yukos and appropriate its valuable assets.” The ruling also stated:

... the Tribunal concludes that this episode provides yet more compelling evidence that the Russian Federation was not involved in a true, good faith tax collection exercise but rather was intent on confiscating the most valuable asset of Yukos and effectively transferring it to the Russian State.

The Tribunal ordered Russia to pay the Yukos shareholders damages of \$50.021 billion, interest of \$5.355 billion and legal costs of \$60 million.

Next steps?

The Russian Federation will appeal the ruling under Dutch arbitration law. Eventually, the arbitration awards are subject to recognition and enforcement under the New York Convention of 1958, which has been signed by over 150 countries. No one expects Russia to voluntarily pay the more than \$50 billion, however. Collection will require seizing and selling Russian commercial assets around the world.

I've never collected more than \$4.25 million in an international case. Even if you want to talk about your claim for less than \$50 billion, I'll answer the phone.

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