Legal Observations on the Yukos Affair: Part V
By Peter Clateman
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I. Introduction

This comment is the next in a series of analyses of legal aspects of the Yukos affair distributed on Johnson's Russia List starting in November 2003.

For previous comments see: JRL #7462 (summary and analysis of the criminal indictment against Khodorkovsky); #8170, #8171 (summary and analysis of criminal indictment against Lebedev with review of some of the proceedings); #8204 (short comment on the order of the Moscow court freezing Yukos's assets); and #8353 (review of the tax claims against Yukos based upon press reports.

This comment will cover certain recent events in the saga:

+ Yukos's filing for bankruptcy protection in federal court for the Southern District of Texas and its receipt of a temporary restraining order against Gazpromneft prohibiting it from participating in the auction of Yuganskneftegaz ("Yugansk") and against various banking institutions prohibiting them from financing the bidders in the auction.

+ The auction by the Russian bailiff of a controlling stake of Yugansk belonging to Yukos.

+ More vocal and concrete threats by Menatep that it will seek damages in international arbitration from the Russian government for bringing and prosecuting tax claims against Yukos in violation of Russian law and international norms.

I intend to distribute a further comment in the near future which will provide an updated analysis of the tax claims themselves. This update is called for since I have received a copy of the "Resolution", dated April 14, 2004, issued by the Russian tax authorities ("MNS") against Yukos which forms the basis of the tax claims against Yukos for the year 2000. This document also contains the objections to the assessment raised by Yukos in the course of the tax review.

Please contact me at pclateman@spkgroup.com if you would like a copy of past comments and cannot find them on the Internet. I am also glad to provide upon requests via e-mail rough translations of the Khodorkovsky and Lebedev indictments, a translation of the Resolution mentioned above and a chart summarizing the legal proceeding in the Yukos affair which is up to date as of December 24, 2004.

II. US Bankruptcy Proceedings

On December 14, 2004, Yukos filed for Chapter 11 bankruptcy protection in the federal bankruptcy court for the Southern District of Texas. As a result of the filing, an automatic stand-still goes into effect that prohibits the company's creditors from taking action against its assets. In addition to making this filing, Yukos sought and received a temporary restraining order ("TRO") against Gazpromneft ordering it not to participate in the auction for share in Yukos's subsidiary, Yugansk. The TRO also prohibited certain banks from financing any of the bidders in the auction. The TRO

effectively expands the scope of the stand-still imposed by the bankruptcy filing by extending it to parties that would not clearly be covered by the stand-still.

A. Jurisdiction, Venue and Forum Shopping

The consensus of commentary in the western press regarding the Yukos bankruptcy filing is that the Texas court lacks jurisdiction over the bankruptcy since it appears that Yukos has minimal assets in, and lacks other contacts with, the jurisdiction. Furthermore, the presence of these assets and certain other contacts with the jurisdiction (such as the presence of Bruce Misamore, Yukos's CFO, in Texas [1]) seem to have been established only on the eve of the bankruptcy filing.

I will not attempt to analyze here in detail the question of jurisdiction (which is primarily one of "subject matter jurisdiction"). I will note, however, it is possible that the court will be influenced in its consideration of the jurisdiction question (even if review of assets in and contacts with the jurisdiction weigh heavily in the court's decision) by its view regarding whether Yukos is improperly seeking to take advantage of US laws or is seeking a forum in which it may expect to receive a fair hearing. Moreover, the question of "venue"—whether or not, even if there is jurisdiction, the US court is the proper place to decide issues of the bankruptcy—will most certainly rest on heavily on this consideration.

Although Yukos's assets and other contacts to the US may be seen as sufficient to establish jurisdiction for the bankruptcy, the court may nevertheless refuse to find jurisdiction if it believes that Yukos is "forum shopping"—that is, Yukos is seeking bankruptcy in the US courts primarily because the rules are more favorable for its purposes. And there are some important differences between Russian and US bankruptcy law which raise a strong suspicion of forum shopping in the current case. Chapter 11 protection is attractive to Yukos's managers and its main shareholders, with whom they appear to be closely aligned, because it is far more difficult for management to be removed under Chapter 11. In fact, a US court would most likely let current managers run the company without significant ongoing interference for some time. While Russian bankruptcy law, like US law, is directed at helping insolvent companies restructure, creditors basically control the Russian bankruptcy process and management is often relieved of authority entirely. In Russia, one would expect that Yukos would be managed under insolvency procedures by a supervisor nominated by the tax authorities and confirmed by the court.

Yukos, anticipating charges of forum shopping, justifies its application to the US courts by setting forth its "big picture" version of the entire Yukos saga. This version, which it has been putting forth in its massive PR campaign of the last year, holds that there is no justice for Yukos in Russia and that its current financial crisis is the result of a government vendetta against it which violates Russia law and international norms. If Yukos is able to convince the court of this big picture view, it would serve as a legitimate argument for the court to find jurisdiction despite the fact that it may otherwise view Yukos's actions as forum shopping. Seeking justice is a legitimate form of forum shopping.

One of the participants in the proceedings, Deutsche Bank, has in fact made the charge of forum shopping against Yukos. However, neither Deutsche Bank nor any other party to the proceedings has directly addressed Yukos's claims that it is seeking justice. That is, I have not seen in the papers any challenge to Yukos's fundamental assertions—that Yukos's actions with respect to taxes were in fact legal, that the prosecution of the tax claims violates international norms and that it is politically motivated. So far, Yukos's assertions on this front are unchallenged.

B. Impact of US Bankruptcy Filing

1. Standstill

As noted above, so long as jurisdiction is maintained over Yukos in its bankruptcy filing, the stand-still against Yukos's assets will remain in place. This is true even if the court does not find that it is the proper venue for deciding any further matters related to the bankruptcy. This stand-still is worldwide and subjects any party violating it to sanctions by the US court. We may therefore expect Yukos to try to take action against Baikal Finance Group for its acquisition of Yugansk through the auction as well as against Rosneft for acquiring Baikal Finance and also against other parties that aid these transactions or participate in further deals regarding Yukos's assets. However, unless such parties have assets in the US, such actions will only have direct effect if Yukos can get the US standstill enforced abroad.

Enforcing the standstill or an order granted to support the standstill outside of US jurisdiction would depend on whether the foreign court would grant "comity" to the US court decision. (Yukos cannot demand recognition of US bankruptcy rulings in foreign courts on the basis of a treaty since the US is not a party to any relevant treaties.) The principle of "comity" says that courts around the world should generally help each other get their decisions enforced unless the foreign decision violates some basic principle of local law or unless the foreign decision was arrived at without application of due process. Due to the differences in bankruptcy regimes around the world, bankruptcy is an area in which comity is not as likely to be given as in other areas of law. While Russian law does recognize comity in theory, it is almost unheard of in practice and, given the differences between Russian and US bankruptcy law, this is not a case in which comity is even theoretically likely. I would guess that Yukos also will find it difficult to get European courts to grant comity to the US order, although its chances in Europe are not entirely remote.

Despite its difficulties in getting foreign courts to enforce the US-imposed stand-still and any orders issued in connection with it, Yukos may view this proceeding as providing certain other advantages (assuming that jurisdiction is found). The US proceeding will provide Yukos with a forum to continue to make its case, even if only for PR effect, that it is not getting justice in Russia. If no counterparty challenges the main points of its "big picture" version of the Yukos saga, Yukos may even secure further decisions that, to some extent, are based upon its version of events. Such decisions may be of value to Yukos in bolstering the credibility of its "big picture" view of events, which it clearly intends to use in other proceedings—its case before the European Court of Human Rights and the other arbitrations it is seeking to bring.

On the other hand, Yukos has nothing to gain by facing off with a counterparty that challenges its "big picture" version of the story at this time. If it manages to maintain the US bankruptcy proceeding, it will receive court decisions that are difficult to enforce. If it loses, it then risks having its "big picture" version of the Yukos saga questioned before it even reaches the human rights and arbitration proceedings which presumably are more important to its cause. Therefore, I would expect Yukos to have second thoughts about pursuing the US bankruptcy proceedings aggressively if its version of the larger story comes under challenge in those proceedings. However, it does not appear that any of the counterparties at this point wishes to address Yukos on this level.

2. Need for a Russian Bankruptcy

If the bankruptcy proceeds in Texas, the court would normally expect Yukos to seek bankruptcy protection in Russia as well since that is where most of its assets are located. If management fails to take such action, interested parties may seek to get the US court to order such action or take other action against management.

The proceedings so far appear to have touched only briefly upon Yukos's plans regarding seeking bankruptcy in Russia. Yukos's position appears to be that no bankruptcy filing in Russia will be necessary since it expects to challenge successfully the main claims that are causing its current insolvency—the tax claims for over $25 billion made against it and its subsidiaries by the Russian tax authorities. Yukos's position is that it has a right to refer this dispute to international arbitration and that it will win such arbitration. Consequently, either the tax claims will be withdrawn or compensation in the amount of the claims paid will be returned. Once this happens, Yukos will not be insolvent and the bankruptcy proceeding may end. This argument has some logic, but it rests upon a rather long chain of argument which depends on a dense set of factual assertions. The propositions that Yukos has a right to arbitration and that it will win such an arbitration are discussed below.

In any event, Yukos has not yet addressed the issue of why it does not plan to seek bankruptcy protection in Russia while such an arbitration proceeds.[2] One may presume that its answer, once again, is the lack of justice for Yukos in Russia.

Regardless of whether the US court requires Yukos to file for bankruptcy in Russia, Russian law itself obligates Yukos's managers to file for bankruptcy if the financial state of the company does in fact indicate that it is bankrupt. Of course, by filing for bankruptcy in the US, Yukos has clearly admitted that this is the case.

As I noted in my previous comment on the tax claims, the current situation in which Yukos is being dismantled by the bailiff is an artificial one caused by Yukos's failure to declare bankruptcy. Initiation of bankruptcy (in Russia) would stop collection of all debts, including the tax claims, and would prevent the sale of Yukos's property to satisfy claims—that is, bankruptcy in Russia would have stopped all enforcement actions (including the Yugansk auction) and provided protection quite similar to that sought by Yukos through its US Chapter 11 filing. It would also prevent interest and penalties from accumulating further on outstanding debts, including the massive penalties that were assessed by the bailiff when Yukos failed to pay the tax judgments for 2000 and 2001. Therefore, it would seem that refusing to file for bankruptcy in Russia (where more practical protection is available) has caused immense damage to Yukos. The US Chapter 11 filing could effectively serve as "exhibit number one" in a case against Yukos's managers in Russia for failing to fulfill their duty to take Yukos into bankruptcy to protect its assets.

Declaring bankruptcy when the financial condition of the company does not truly call for it can also lead to liability for managers under Russian law. If managers take a company into bankruptcy even though the company is solvent or if the company has not taken appropriate measures to contest false claims against it, then the managers may be held liable. Articles appearing in the Russian press this fall have quoted Yukos sources as stating that Yukos's managers had not filed for bankruptcy due to threats from the government that it would prosecute Yukos managers for false bankruptcy if they took such a step. I have seen no independent sources quoted regarding possible accusations of "false bankruptcy" and there is no reference to them in Yukos's court papers to date.

"False bankruptcy" has been a popular method in Russia over the past few years for delaying payment of tax. Such bankruptcies are "false" in the sense that the company is actually able to pay its debts and that the bankruptcy is brought and controlled by "friendly" creditors, who hold debt that has been generated simply for the purpose of causing bankruptcy (that is, this is not debt that is expected to be repaid). This hardly describes the Yukos situation, so it is not clear how an accusation of false bankruptcy could be supported. However, such threats, if they are truly being made, would clearly constitute part of the lawless campaign which Yukos alleges the government is waging against it.

II. Auction of Yugansk

1. Basis for Auction

In my previous comments in September, I noted that the main valid objection to a sale of Yugansk to satisfy tax claims against Yukos was that the value of Yukos's shares in this subsidiary was clearly far in excess of the outstanding unpaid judgments against Yukos which were subject to collection at the time.

It does not appear, however, that Yukos has objected to the sale on the grounds that the value of the asset was not commensurate to the unpaid judgment. Rather, it objected to the sale on the grounds that its share in Yugansk constituted a "production asset", which Russian law says should not be selected for sale "in the first order" by the bailiff to satisfy unpaid judgments. As I discussed previously, Yukos's shares in Yugansk do not appear to constitute a "production asset" under Russian law and therefore this objection does not appear to be valid.

Even if Yukos had successfully argued (against a strict reading of the law) that a controlling stake in Yugansk should be considered a "production asset" because it is integral to the production activities of the Yukos group, it is not clear what other material assets Yukos (a holding company) has that the bailiff could sell other than shares in the production subsidiaries. In other words, even if Yukos won this legal point, it is likely that shares in Yugansk or other production subsidiaries would have to be sold anyway to satisfy the claims. [3]

Therefore, the main question regarding the selection of Yugansk for sale by the bailiff remains whether the value of Yukos's 76.3% stake in this company is comparable to the amount of unpaid tax judgments against Yukos. Since Yukos reportedly paid the entire tax judgment for 2000 (some $3.4 billion) by the end of November 2004, the amount of unpaid tax judgments subject to collection at the time of the auction depends on the status of proceedings on the claims for 2001-2003:

<u>Year 2001</u>: The bill for 2001, in the amount of RUR 115 billion (including tax, interest and penalties) appears to have become subject to collection in full by the date of the auction—that is, MNS won its claims in the first instance and this judgment was then upheld (subject to minor adjustments) on appeal. Court judgments in Russia become subject to collection after they are upheld on appeal (or after the initial judgment if no appeal is filed).

<u>Year 2002</u>: The bill for 2002, in the amount of RUR 193 billion does not appear to have been subject to collection in full at the time of the auction. This bill consists of two parts: tax and interest (RUR 121 billion) and fines (RUR 72 billion). Tax penalties assessed by MNS do not become subject to collection (if protested) without a court decision which, if appealed, must be

upheld on first appeal. Based on press reports, it does not appear that a final judgment regarding the penalties for 2002 has come into force. With regard to taxes and interest, the Tax Code provides MNS with the authority (in most cases) to start enforcement of such claims on the basis of its own conclusion. The exceptions to MNS's authority to start such collection include instances in which, to put it generally, the computation of the tax assessment under the Tax Code requires the determination of a fact or legal relationship that only a court may determine (one relevant example is whether entities are "affiliated" other than via shareholding). Without analyzing the issue here, I note that there are good arguments that some or all of MNS's claims against Yukos require a court decision to become subject to collection. Therefore, it is arguable that some or all of the RUR 193 billion tax and interest claim for 2002 was also no subject to collection at the time of the Yugansk auction.

Year 2003: MNS's final order with respect to 2003 does not appear to have been presented to Yukos by the time of the auction. Consequently, there does not appear to be any argument available to assert that this claim was subject to collection.

Based on the foregoing, no more (and possibly quite less) than RUR 236 billion (the 2001 bill plus the tax and interest portion of the 2002 bill) was subject to collection at the time of the auction. This amounts to about $4 billion, which would appear to be significantly less than the value of Yukos's 76.3% stake of Yugansk under any valuation. Therefore, if the status of the claims and court proceeding as reported in the press is in fact accurate, the auction appears to have been premature.

2. Conduct of the Auction

As noted in my previous comment, according to the Law on the Enforcement of Judgments, the bailiff is supposed to complete enforcement actions within two months of receiving either the court decision on execution of the judgment or a valid request for enforcement from MNS (if the claim is subject to collection without a court order as discussed above). Therefore, other than the fact that the bailiff selected an asset clearly worth more than the debt subject to collection as discussed above, the bailiff's moves to sell assets to settle unpaid amounts subject to collection appear to be in accordance with law.

Unfortunately, the law and regulation regarding how the bailiff is supposed to go about selling the assets are sparse. The Law on the Execution of Judgments merely states that such sales shall be carried out by a "specialized organization" on a commission or other contractual basis. No definition of "specialized organization" is provided, nor are the terms of the sale procedure. By government decree, dated April 19, 2002, the State Property Fund has been designated as the "specialized organization" to carry out the sale of such property when the government is the creditor. Therefore, it is correct for the State Property Committee to have conducted the auction of arrested Yugansk shares. However, the State Property Fund's own internal regulation, dated November 29, 2001, on how such sales are to be conducted hardly define the process in any substantive detail.

Before the auction, there had been much speculation in the press regarding whether a minimum price would be set, what that price would be and whether it would be based upon the valuation of Yugansk performed at the request of the bailiff by Dresdner Kleinwort Wasserstein. The State Property Fund rules do not clearly require that any valuation be carried out of the asset to be sold or that any starting price be set for the auction. The valuation carried out at the request of the bailiff is carried out at a different stage of the execution process and the law does not clearly link this

valuation to the actual sale (it appears that the purpose of such valuation is for the selection by the bailiff of the property to be sold, not for the purpose of establishing a fixed or minimum sale price). The DKW valuation reportedly provided a range of $14-17 billion for 100% of Yugansk, absent certain contingencies. However, the DKW valuation also indicated a minimum valuation of $10.4 billion in the event that tax claims were filed against Yugansk, which they have been. In the end, it appears that the State Property Fund in fact used this $10.4 billion figure as the auction starting price --$7.98 billion for 76.8% of the equity of Yugansk. The shares were apparently bought by Baikal Finance Group for just over this amount.

Despite technical compliance with a rather loose set of rules, significant grounds could be found to challenge this auction if it can be shown that it was either fixed or that no real effort was made to get the highest price possible under the circumstances. I believe that it is arguable based on the Civil Code that there is a duty on the part of those conducting an auction to make a real effort to get the highest price possible under the circumstances, including the fact that the bailiff is required to try to satisfy the creditors claims within two months according to the Law on the Execution of Judgments. Obviously, allowing or even participating in collusion among the bidders would violate such a duty. Furthermore, under the rules of the State Property Fund, the auction requires two bidders and collusion would indicate that there were not two bidders in reality, which should be grounds for invalidating the auction.

The difficulty of establishing collusion in this bidding process should not be overestimated. The press has contained various reports that the government discouraged a number of serious foreign bidders from participating in behind the scenes discussions. Furthermore, the prequalification of unknown shell companies, which all appear to have acted with the knowledge, if not under the instruction, of government, would suggest the entire auction was a piece of staged theater. Demonstrating collusion of this type in a civil court would not require some sort of official document or a tape recording of responsible officials specifically demonstrating collusion. Depending on what more is revealed about Baikal Finance Group, the other bidders and Gazprom's own behavior in the auction, Yukos may be well on its way to having available sufficient evidence to demonstrate that it was more likely than not that collusion took place, which is all that should be necessary to challenge the auction or sue for damages before in an unbiased proceeding. As many other commentators have noted, this auction bears ironic similarity to the sham privatization auctions of the 1990s, examples of which are described in the criminal indictments against Khodorkovsky and Lebedev.

The low sale price, however, received for Yugansk is not in itself proof that the auction was invalid. The efforts of Menatep and Yukos to scare off potential bidders and financing parties with threats of litigation may have been successful and affected the competitiveness of the bidding. A number of banks apparently obeyed the Texas court's order and did not participate in financing participants in the auction. Even if such parties, to avoid legal attack, agreed to resume discussion of acquiring a stake Yugansk at a later date, this would not necessarily constitute improper collusion or a reason to invalidate the auction.

III. Yukos's Search for a Forum

Yukos and its core shareholder, the Group Menatep, have increased the frequency and volume of their threats to seek damages from the Russian government for what they claim is a politically motivated attack on Mikhail Khodorkovsky and his assets. As indicated in Yukos's filing in Texas, it believes that the "main" proceeding will be some form of international arbitration against the

Russian government that will recover for Yukos the "damage" caused by the tax claims. Yukos has cited the Russian Law on Foreign Investment as giving foreign shareholders in Yukos the right to arbitrate their disputes with the Russian government through some form of international arbitration. This is a controversial reading of the single provision of the law that mentions arbitration (although it should be acknowledged that other have tried this interpretation). The accepted and straightforward interpretation of this provision is that it merely confirms that, if Russia has a treaty covering the arbitration of investment disputes, then the foreign investments described in this law may also be subject to arbitration under such treaty. Therefore, Yukos still needs to find a treaty giving it the right to arbitrate with the Russian government.

A number of possible treaties have been mentioned—human rights conventions, bilateral investment treaties and the Energy Charter. Rather than attempting to take on the task of analyzing possible claims under each relevant agreement, I will discuss below what seem to be two necessary elements that Yukos must show in order to win an action under any of the possible relevant international agreements.

First, Yukos would have to show that it is simply not guilty under Russian law of massive tax evasion. The thrust of my earlier comments has been that the fundamental factual allegations against Yukos and against Khodorkovsky and Lebedev as well, constitute rather blatant forms of tax evasion and fraud under just about any modern legal system. I note that few of the material facts asserted by the prosecutors or the tax authorities have been disputed by Yukos, Khodorkovsky and Lebedev. [4] Therefore, Yukos is making a rather unappealing argument—that these blatant and bold maneuvers were somehow legal in Russia at the time. However, as set forth in my previous comments, I do believe that Russian law viewed the various tax maneuvers as illegal at the time—there are even various ways in which they may be viewed as illegal. [5] As I have also noted, in some instances, the prosecutor and tax authorities may have formulated their claims in a manner that is not entirely sound, but this is a problem with how the claims have been formulated, not with the facts or with Russian law.

Yukos argues that even if its actions were theoretically illegal, they were legal *de facto*. To make such an argument, I think Yukos will have to show more than that "everyone was doing it". It will also have to show that there were virtually no known examples of enforcement of such laws and/or that there had been official indication that such activities were not going to be treated as illegal. However, tax claims for similar transfer pricing schemes or for the misuse of on-shore tax havens were not unknown at the time, even if many of the largest violators escaped liability. Yukos may attempt to make such an argument anyway, but it is a very unappealing argument given the blatant nature of the actions themselves. Yukos has also prominently referred in court and its PR to the fact that its activities passed numerous tax audits, which it claims indicates that its activities were legal. But these audits of individual entities were clearly conducted without knowledge of relevant facts, revealed in later investigations, demonstrating how the various entities acted as part of an overall scheme. Furthermore, anyone with practical knowledge of the audit process in Russia would have serious questions regarding how such clean audits were obtained. If, as I have argued, the tax schemes violated the letter of the law, then it will be difficult for Yukos to argue that these past tax audits and the lack of widespread prosecution of such activity constituted an official statement of the law on which it should be entitled to rely.

Furthermore, Yukos's argument that its actions were legal at the time could be seriously undermined by any evidence that it employed bribery to carry out its schemes. Obviously, bribery would tend to be employed to further an illegal scheme rather than a legal one. In my comments to the Lebedev

indictment earlier this year, I noted that it was disappointing, given that such illegal activity was being conducted with the knowledge and complicity of various officials, that the indictment did not "name names" and that we had yet to see any serious attempt to go after the officials who must have participated in the various crimes charged. Since that time, however, there has been some movement in this direction—the head of one of the "on-shore tax havens" used by Yukos has been charged with corruption in connection with granting tax breaks to Yukos, which the authorities claim were granted and used illegally. If this case and other prosecutions of officials go forward, it will seriously damage claims that Yukos and Menatep acted legally. Of course, such evidence would also reduce Yukos's appeal as a victimized plaintiff.

Rather than argue that its behavior with respect to paying taxes was legal (*de facto* or *de jure*) at the time, Yukos may argue that it is being treated unjustly because the punishment being sought is unheard of and out of proportion—the proverbial book is being thrown at it. As I discuss below, I believe that this would only give Yukos a "hook" to make a claim under a relevant investment or human rights treaty if the book is being thrown at it for an inappropriate reason. Intransigence in dealings with the authorities, lack of contrition and cooperation and, to a certain extent, evidence that the scope of its illegal activity was broader than the particular charges brought are legitimate reasons for throwing the book at Yukos. Tax charges have often served as a proxy for punishing a broad range of underlying illegal activity through one, more simple prosecution. The prosecution of Al Capone for tax evasion became a tactical model for fighting organized crime in the US. Public comments from the authorities indicate that the authorities wish to draw a parallel to efforts to fight organized crime through tax claims in other countries.

The second element that Yukos would need to show in order to get relief under any international agreement is that it has been mistreated for an inappropriate reason. In other words, international arbitration treaties generally do not offer a right to arbitration simply as a higher level appeal to a national court. Under a human rights treaty, in order to claim compensation, Yukos or its shareholders would have to show not only that the Russian courts were improperly imposing tax claims, but they were doing so as a punishment for exercising protected rights (such as legitimate political activity). Under a bilateral investment treaty, Yukos or its shareholders would have to show that the purpose of the improper tax case is to confiscate property in violation of the investment protections provided in the treaty.

Yukos has claimed both that the tax cases are punishment for political activity of Khodorkovsky and that they represent an illegal confiscation without compensation carried out to further a general plan to renationalize the Russian natural resources sector. If Yukos passes the previous hurdles described above, the element of "ulterior motive" may not be that difficult to establish. One should not overestimate the amount of evidence that would be needed to win this point in an arbitration. Such ulterior motives need not be shown by direct testimony or documents confirming the existence of such a scheme and naming its participants. An international arbitration panel would simply be seeking to determine whether it is more likely than not that such motives are behind the unfair treatment of Yukos. The public record on the Yukos affair already contains many points that would help Yukos establish the likely existence of such ulterior motives. For example, President Putin's public statements after the Yugansk auction basically proclaimed that the sale of Yugansk back to the state represented some sort of ultimate justice for earlier violations in the privatization process. While such comments may be spun in different ways, Yukos will undoubtedly refer to such comments as an admission of improper ulterior motives by the government in the entire process (that is, nationalization without compensation).

While Yukos faces tremendous hurdles in securing any form of compensation through international arbitration (including questions of the applicability of each particular international arbitration agreement, which I have not even started to address here), Yukos is currently running a one-sided show which is helping it to build momentum for such claims. If it continues to run unopposed both in the press and in the courts, it will make challenging its story more difficult at a later stage. This story is essentially that: (a) Yukos's founders are successful "entrepreneurs"; (b) Yukos's founders "built" Yukos into one of Russia's leading oil companies; (c) Yukos became a "transparent, western-style business" under Khodorkovsky and his team; (d) Khodorkovsky became involved in "politics"; (e) the tax and other claims brought against Yukos and Khodorkovsky are invalid under Russian law and violate international norms; and (f) these claims have been brought as a punishment for Khodorkovsky's legitimate political activity and/or simply to renationalize the oil company without paying compensation. Unless an interested party steps forward and challenges each element of this story, Yukos chances of finding a forum and eventual relief could be significant.

Footnotes:

1. None of the parties that have challenged the jurisdiction of the court have specifically raised the issue of Bruce Misamore's real authority in the company. While Bruce Misamore is referred to generally as Yukos's CFO, it is not clear what formal role he plays in Yukos's management structure since the role of the executive body of Yukos has been transferred to Yukos-Moskva. It does not appear that Mr. Misamore is a CFO as that position would be understood in a US company, which may diminish the relevancy of his presence in Texas for the purpose of establishing jurisdiction.

2. Yukos told the Texas court that granted the TRO that Yukos could not declare bankruptcy in Russia without a shareholders meeting, which had been schedule to take place only after the Yugansk auction (although this meeting has now been further postponed due to a successful challenge to the convocation of the meeting launched by Sibneft). This statement regarding Russian law, however, is not true. The management has the authority and duty to apply for bankruptcy without shareholders approval under Russian law; the board, by way of it oversight of the management, has the authority and duty to ensure that management acts appropriately in this manner as well. In fact, Yukos applied for bankruptcy in the US without a shareholders decision, which obviously confirms its authority to do so.

3. Yukos also attempted to argue that its shares in Sibneft, which constituted a minority stake, were not a "production assets" since Sibneft had not yet become integral to the company's activities, and that therefore these shares should be sold by the bailiff first. However, as pointed out in my previous comment, this request did not constitute a reasonable proposal since Yukos's ownership of its Sibneft shares was under dispute due to the unwinding of its merger with Sibneft and these shares were frozen under a separate court order brought by Sibneft's shareholders.

4. The main factual dispute related to the tax claims appears to be Yukos's claim that it is not affiliated with certain entities involved in the alleged tax evasion schemes. This is actually a mixed "fact and law" dispute in which Yukos disputes certain facts that establish its control over these companies and argues that without such facts, the companies cannot be considered "affiliated". However, Yukos does accept that it is affiliated with a number of the companies used in the scheme, so it does not dispute the factual basis of a number of the tax claims. As noted in my previous

comment, Yukos's claim that it is not affiliated with entities through which billions of dollars of its revenue and profit were channeled is an interesting tactic.

5. As noted in the introduction, I intend to update my previous analyses of the tax claims based on the actual text of the tax claims for 2000, which I received recently.