IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

Yukos Capital Limited
(f/k/a Yukos Capital S.à.r.l.),

Petitioner,

v.

The Russian Federation,

Respondent.

Civil Action No. 22-cv-00798

Declaration of Matthew S. Rozen in Support of Petition to Enforce Arbitral Award

EXHIBIT B

ARBITRATION PURSUANT TO THE RULES OF

THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW

(1) Yukos Capital S.a.r.l. (Claimant)

- and -

(2) The Russian Federation (Respondent)

NOTICE OF ARBITRATION

---

15 February 2013

GIBSON, DUNN & CRUTCHER LLP

Telephone House
2-4 Temple Avenue, London EC4Y 0HB
020 7071 4000 020 7071 4244 *Fax*

Contents

Page

I. Introduction 1

II. The Parties 1

III. Proposal as to the Number of Arbitrators AND PLACE OF ARBITRATION 2

IV. General Nature of Yukos Capital's Claims 3

A. Yukos Capital's Investments 4

B. The Expropriation of Claimant's Investments 6

(i) The Dismantling and Destruction of Yukos 6

(ii) Acts Directed at Yukos Capital 8

V. The Energy Charter Treaty 10

VI. The Tribunal's Jurisdiction 12

A. Yukos Capital is an Investor 12

B. Russia is a Contracting Party for Purposes of this Proceeding 13

C. The Dispute Relates to Investments Made by Yukos Capital in Russia 14

D. The Dispute Concerns Alleged Breaches of Russia's ECT Obligations 15

VII. The Expropriation of Yukos Capital's Investments 15

A. The Dismantling and Destruction of Yukos Oil 15

(i) The Politically Motivated Attacks Begin 17

(ii) The Attack Expands to Yukos 22

(a) The Tax Re-Assessments 22

(b) The Enforcement Story 38

(c) The Forced Auction of Yuganskneftegaz 44

(d) The Forced/Sham Bankruptcy of Yukos Oil 49

(e) Conclusion 55

B. Illegal Acts Directed at Yukos Capital 56

VIII. Yukos Capital's Claims and Requests for Relief 68

A. Claimant's Principal Claim 68

B. Claimant's Alternative Claim 69

C. Yukos Capital's Request for Relief........ 70

I. INTRODUCTION

1. Yukos Capital S.a.r.l. ("*Claimant*" or "*Yukos Capital*") hereby demands arbitration against the Russian Federation ("*Respondent*" or "*Russian Federation*") under the Arbitration Rules of the United Nations Commission on International Trade Law (as revised in 2010) (the "*UNCITRAL Rules*").[1] The agreement to arbitrate on which Yukos Capital relies is set forth in Article 26 of the Energy Charter Treaty of 1994 (the "*ECT*").[2] In this proceeding, Yukos Capital seeks compensation for illegal acts attributable to the Russian Federation which expropriated, treated in a discriminatory fashion and otherwise failed to protect Yukos Capital's investments in Russia.

2. This Notice of Arbitration is submitted pursuant to Article 3 the UNCITRAL Rules. Yukos Capital reserves the right to amend and/or supplement the matters and claims addressed herein.

II. THE PARTIES

3. Claimant Yukos Capital is a company organised and existing under the laws of Luxembourg and at all relevant times carried out business as a finance company.[3] Claimant's registered office is as follows:

   46A, Avenue J.F. Kennedy
   L-1855 Luxembourg P.O. Box 415
   L-2014 Luxembourg

4. Claimant is represented in this proceeding by Gibson, Dunn & Crutcher LLP. Communications should be directed as follows:

---

1 Claimant notes that, under Article 1(2) of the UNCITRAL Rules, it is not presumed that the 2010 revised rules are to apply given that the Respondent's offer to arbitrate was made prior to 15 August 2010. Article 26(4)(b) of the Energy Charter Treaty is silent on this point. In the circumstances, the Claimant proposes that the 2010 revised rules apply but appreciates this may be a matter of discussion with the Respondent and the Tribunal.

2 A copy of the ECT is annexed to this Notice of Arbitration as Exhibit C1. References herein to "Exhibit C__" or "Ex. C__" are to the annexed exhibits.

3 Registry excerpt from the Luxembourg Chamber of Commerce dated 11 September 2012 (Exhibit C117).

Cyrus Benson
Gibson, Dunn & Crutcher LLP
Telephone House
2-4 Temple Avenue
London EC4Y 0HB
UK
Phone: +44 207 071 4000
Fax: +44 207 071 4244
Email: cbenson@gibsondunn.com

Laurence Shore
Gibson, Dunn & Crutcher LLP
200 Park Avenue
New York, New York 10166-0193
USA
Phone: +1 (212) 351-4000
Fax: +1 (212) 351-4035
Email: lshore@gibsondunn.com

5. The Respondent is the Russian Federation. Respondent will in due course indicate how it wishes communications to be addressed for purposes of this arbitration. This Notice of Arbitration has been served on the following:

Government of the Russian Federation
Krasnopresnenskaya nab., 2
103274, Moscow
Russian Federation

Administration of the President of the Russian Federation
Staraya ploshchad, 4
103132, Moscow
Russian Federation

Administration of the President of the Russian Federation
ul. Ilyinka 23, pod. 11
103132, Moscow
Russian Federation

Ministry of Justice of the Russian Federation
Zhitnaya ul., 14, STR. 1
119049, Moscow
Russian Federation

III. PROPOSAL AS TO THE NUMBER OF ARBITRATORS AND PLACE OF ARBITRATION

6. Pursuant to Article 3(3)(g) of the UNCITRAL Rules, Claimant proposes that three arbitrators be appointed to constitute the arbitral tribunal.

7. Pursuant to Articles 3(4)(c) and 9(1) of the UNCITRAL Rules, Yukos Capital hereby appoints J. William Rowley Q.C. as one of the three arbitrators. Communications to Mr. Rowley may be directed to:

J. William Rowley Q.C.
20 Essex Street
London
WC2R 3AL
Phone: +44 20 7842 1200
Fax: +44 20 7842 1270
Email: wrowley@20essexst.com

8. Pursuant to Article 6(1) of the UNCITRAL Rules, the Claimant proposes that the Secretary-General of the Permanent Court of Arbitration at The Hague serve as appointing authority.

9. Pursuant to Article 18(1) of the UNCITRAL Rules, if the parties have not previously agreed on the place of arbitration, it "*shall be determined by the arbitral tribunal having regard to the circumstances of the case*". In this regard, Article 26(5)(b) of the ECT provides that "*any arbitration under this Article shall at the request of any party to the dispute be held in a state that is a party to the New York Convention*". Claimant proposes that the place of arbitration be The Hague, Netherlands.

IV. GENERAL NATURE OF YUKOS CAPITAL'S CLAIMS

10. Claimant Yukos Capital is a former, indirect, wholly owned subsidiary of Yukos Oil Company OJSC ("*Yukos Oil*" or "*Yukos*"). It ceased to be such in November 2007 when Yukos was dissolved at the conclusion of formal bankruptcy proceedings in Russia. At its formation, Yukos Capital's parent was Yukos Finance B.V., a Dutch holding company wholly owned by Yukos Oil. In April 2005, a restructuring was carried out whereby protective measures were implemented in an effort to prevent the foreign assets of Yukos Oil from being confiscated by the Russian State. These measures included transferring ownership of Yukos Capital to Yukos International B.V., a Dutch holding company which holds certain of the former international assets of Yukos Oil, and interposing a Dutch trust between Yukos International and Yukos Finance.

11. To date, this strategy has succeeded, in large part due to the refusal of the Dutch courts to recognise the Yukos bankruptcy in the Netherlands:

> *"the Russian bankruptcy order in which Rebgun was appointed receiver in the bankruptcy of Yukos Oil was effected in a manner not in accordance with the Dutch principles of due order of process and is thus in violation of the Dutch public order. For that reason, the bankruptcy order cannot be recognised and the receiver's powers that ensue from it under Russian law cannot be exercised by Rebgun in the Netherlands."*[4]

The above-mentioned protective measures, coupled with the Dutch court's ruling, have preserved Claimant's ability to bring these claims.

12. This dispute concerns approximately USD 3.0 billion in loans (exclusive of interest and penalties)[5] made by Yukos Capital to Yukos Oil, the Russian Federation's illegal expropriation of that investment (both directly and indirectly), and the Russian Federation's unfair and discriminatory treatment of Yukos Capital. The acts of which Yukos Capital complains, which are to be attributed to the Russian Federation, include: (i) the dismantling, dissolution and ultimate removal of Yukos Oil from the companies register in Russia, thus rendering it unable to repay Yukos Capital and reducing the value of Yukos Capital's investment to zero; and (ii) the arbitrary and capricious refusal to recognise Yukos Capital's claims to repayment in the orchestrated "bankruptcy" of Yukos Oil (coupled with the recognition of claims by similarly situated creditors).

13. The claims in this case are not brought on behalf of Yukos Oil, nor are the claims brought on behalf of former shareholders of Yukos Oil. It is public knowledge that Yukos Oil initiated its own claims before the European Court of Human Rights prior to the company's demise and that certain of Yukos Oil's former shareholders have brought claims before tribunals constituted under investment treaties. Yukos Capital's claims are distinct and relate to discrete investments made by Yukos Capital and the damage suffered by it as a result of the expropriation of those investments.

A. Yukos Capital's Investments

14. By the start of 2004, Yukos Oil was by all accounts one of the, if not the, most successful oil companies in Russia. Yukos and its subsidiaries were the largest

---

[4] Judgment of the District Court of Amsterdam, 31 October 2007 (LJN BB6782), page 19. (Exhibit C95).

[5] Based on a RUR/USD exchange rate of 30.0277/1 as reported by the Central Bank of Russia on 31 January 2013.

producers of crude oil in Russia and the largest exporters of crude oil from Russia. Together they produced slightly less than 20% of all the crude oil produced in Russia, and refined and marketed slightly less than 20% of the refined products in Russia. This made Yukos Oil one of the largest oil and gas companies in the world. In 2003, for example, Yukos' production was 80.8 million metric tons (591 million barrels) of crude oil and gas condensate, more than that produced by ChevronTexaco, TotalFinaElf, or the country of Libya as a whole. As late as April 2004, Yukos' market capitalisation was estimated at over USD 40 billion.

15. Yukos Capital was incorporated in Luxembourg on 31 January 2003 as a "*société à responsabilité limitée.*" Its intended purpose was to serve as a vehicle to provide financing to international companies within the Yukos group engaged in merger and acquisition activities. While Yukos Capital engaged in certain such activities, as events transpired, by far the largest recipient of financing from Yukos Capital was Yukos Oil.

16. Throughout much of 2003, Yukos Oil was engaged in a major expansion process which included a series of important mergers with other major oil and gas companies. One of these transactions was the merger of Yukos Oil and Sibneft, then Russia's fifth largest oil company. The merger was legally completed on 4 October 2003, with YukosSibneft on track to become the world's fourth largest oil company (the merger was later derailed by the Russian State).

17. The Yukos-Sibneft merger was structured as a cash purchase by Yukos of 20% of Sibneft's outstanding stock coupled with an exchange of new Yukos shares for Sibneft's remaining shares at an agreed ratio. In connection with the merger, Yukos sought financing from a number of sources both outside and within the Yukos group. These sources included Yukos Capital.

18. More specifically, pursuant to a loan agreement dated 2 December 2003 (the "*December 2003 Agreement*"),[6] Yukos Capital agreed to loan Yukos an amount not to exceed RUR 80 billion (USD 2.7 billion).[7] Interest was to be paid quarterly at a rate

---

6 Exhibit C9. An addendum to the December 2003 Agreement was entered into on 27 October 2005 (Exhibit C59).

7 Based on a RUR/USD exchange rate of 29.7037/1 as reported by the Central Bank of Russia on 2 December 2003.

of 9%, with the borrowed principal repaid by 31 December 2008. Any delay in payment entitled Yukos Capital to a penalty in the amount of 0.1% of the amount overdue for each day of delay. During the period December 2003 to June 2004, the RUR 80 billion available under the December 2003 Agreement was disbursed to Yukos in full.

19. Pursuant to a second loan agreement dated 19 August 2004 (the "*August 2004 Agreement*"),[8] Yukos Capital agreed to loan Yukos an amount not to exceed USD 355 million. Unlike the first loan, originally intended for use in the Sibneft merger, the August 2004 loan was made to assist Yukos in surviving a growing onslaught by the Russian State. Interest was to be paid semi-annually at a rate of six-month LIBOR plus 1.75%, with the borrowed principal repaid by 30 December 2009. Any delay in payment entitled Yukos Capital to a daily penalty in the amount of 0.1% of the amount overdue. The USD 355 million available under the August 2004 Agreement was disbursed to Yukos Oil contemporaneous with the execution of the agreement. (The December 2003 and August 2004 loans are referred to hereinafter as the "*Loans*".)

20. Quarterly interest payments were made by Yukos under the December 2003 Agreement for the quarters ending 31 December 2003, 31 March 2004 and 30 June 2004. Due to illegal acts attributable to the Russian Federation as described below, no further payments were made under either Agreement and, by letter dated November 11, 2005, Yukos Capital communicated a formal notice of default.[9]

B. The Expropriation of Claimant's Investments

(i) The Dismantling and Destruction of Yukos

21. Beginning in mid-2003, in a campaign marked by disregard for the law, the Russian Federation sought to destroy Yukos. In this it succeeded, culminating in the dissolution and removal of Yukos Oil from the Russian companies register in November 2007. The acts of the Russian Federation leading to this result have been

---

[8] Exhibit C30. An addendum to the August 2004 Agreement was entered into on 27 October 2005 (Exhibit C60).

[9] Letter to OAO NK Yukos from Yukos Capital S.A.R.L dated 11 November 2005 (Exhibit C61).

denounced in the world press and have been the subject of numerous legal proceedings. They include, without limitation:

- the arrest, harassment and intimidation of Yukos management and those associated with Yukos (including employees, lawyers and auditors);
- the disruption of Yukos' operations through widespread and invasive searches and seizures;
- threatened revocation of Yukos' oil licenses;
- the break-up of Yukos' merger with Sibneft;
- charging Yukos with massive, unprecedented and wholly unwarranted tax liabilities based on spurious re-assessments;
- the freezing of Yukos' assets to make payment of the alleged tax claims impossible;
- the seizure and expropriation of Yuganskneftegaz, Yukos' largest production subsidiary, and its sham auction at a fraction of Yuganskneftegaz's true value (ultimately to a shell company fronting for state-owned Rosneft Oil Company);
- the forced sham bankruptcy of Yukos despite the fact that Yukos was undeniably solvent (even assuming the validity of the tax re-assessments);
- the expropriation and sham auctions of the remainder of Yukos' Russian assets; and
- the attempts to expropriate and conduct sham auctions of Yukos' non-Russian assets, including Yukos Capital's indirect parent Yukos Finance B.V.

22. With the conclusion of the Yukos bankruptcy in November 2007, Yukos was extinguished as an entity and rendered permanently unable to satisfy its obligations to Yukos Capital. Stated differently, the Russian Federation expropriated Yukos Capital's investment (*i.e.*, its Loans to Yukos Oil).

23. The two investment treaty tribunals to have fully considered the Russian Federation's conduct with respect to Yukos Oil agreed. In *RosInvestCo UK Ltd. v. The Russian Federation*, the Tribunal (V.V. Veeder, QC, Prof. Dr. Kaj Hobér, Dr. Nils Eliasson) concluded that:

> *"...the totality of Respondent's measures were structured in such a way to remove Yukos' assets from the control of the company and the individuals associated with Yukos. They must be seen as elements in the cumulative treatment of Yukos for what seems to have been the intended purpose. The Tribunal, in reviewing the various alleged breaches of the IPPA, even if the justification of a certain individual*

> *measure might be arguable as an admissible application of the relevant law, consider that this cumulative effect of those various measures taken by Respondent in respect of Yukos is relevant to its decision under the IPPA. An illustration is, as Claimant has pointed out, that despite having used nearly identical tax structures, no other Russian oil company was subjected to the same relentless and inflexible attacks as Yukos. In the view of the Tribunal, they can only be understood as steps under a common denominator in a pattern to destroy Yukos and gain control over its assets.*
>
> *....Indeed, it is undisputed that Yukos, as a result of the various measures of Respondent described in the Parties submissions and summarized above in this award, was deprived of its assets and that this affected Claimant's shares in Yukos.*
>
> *...Therefore, the* ***Tribunal concludes*** *that Respondent's measures, seen in their cumulative effect towards Yukos, were an unlawful expropriation under Article 5 IPPA."*[10]

24. Consistent with *RosInvestCo*'s conclusion, the Tribunal in *Quasar De Valores* (Charles Brower, Toby Landau, Jan Paulsson) held:

> *"Based on the extensive record in this proceeding, the Tribunal concludes that Yukos' tax delinquency was indeed a pretext for seizing Yukos assets and transferring them to [State-controlled] Rosneft. As discussed, this finding supports the Claimants' contention that the Russian Federation's real goal was to expropriate Yukos, and not to legitimately collect taxes.*"[11]

(ii) Acts Directed at Yukos Capital

25. The Russian Federation also directed acts at Yukos Capital itself to similar effect. At the behest of State-owned Rosneft Oil Company, the forced bankruptcy of Yukos was commenced in March 2006 on the basis of the purported tax liabilities asserted in tax re-assessments for the years 2000-2003, inclusive. By court order dated 1 August 2006, Yukos was declared bankrupt and formal bankruptcy proceedings were initiated.

26. Despite the commencement of bankruptcy proceedings, Yukos had considerable assets available to satisfy creditors' claims, indeed, assets more than sufficient to satisfy all such claims. Accordingly, on 27 April 2006, Yukos Capital filed an

---

10 *RosInvestCo UK Ltd. v. The Russian Federation* (SCC Arbitration V (079/2005)), Final Award, 12 September 2010, ¶¶ 621, 625 and 633 (Exhibit C109).

11 *Quasar De Valores SICAV S.A. and others v. The Russian Federation* (SCC Arbitration (24/2007), Final Award, 20 July 2012, ¶¶ 177 and 186 (Exhibit C116).

application for inclusion of the Loan claims in the Yukos Registry of Claims. This application was rejected on the unsupported basis that the Loans were not yet due and, on or about 6 October 2006, Yukos Capital filed a second application following commencement of the liquidation phase of the bankruptcy.

27. Submissions in opposition to Yukos Capital's second application to register its claims were made by the court-appointed receiver and the Russian Federal Tax Service. The Tax Service contended that Yukos Capital's loans to Yukos were not valid legal obligations entitling Yukos Capital to creditor standing because the funds loaned to Yukos were its own funds. The Tax Service further argued that this conclusion had already been reached by the courts in prior rulings. On the basis of these submissions, Yukos Capital's application to participate as a creditor was denied by the Russian courts.

28. However:

- no evidence was provided to support the Tax Service's contention (which was not correct);
- no court had determined that the funds loaned to Yukos were its own;
- the submissions of the Tax Service and receiver were not provided to Yukos Capital in advance of the hearing, in violation of Russian law;
- Yukos Capital's counsel was subjected to threats and intimidation leading her to determine that she could not attend the hearing on Yukos Capital's application. This included police raids on her office, the seizure of files and threats to initiate a criminal proceeding against her son in connection with entirely unrelated matters;
- the court was notified of the circumstances giving rise to Yukos Capital's absence from the hearing on its application, and understood that the only objections to the application were those submitted to it *ex parte* on the day of the hearing, but determined to proceed nonetheless, all in violation of the most basic principles of due process; and
- the court's written opinion denying Yukos Capital's application was a "cut and paste" of the Federal Tax Service's *ex parte* submission.

29. Yukos Capital's appeals from the denial of its application were summarily rejected, the appeals courts simply repeating what the court of first instance had said in its opinion (*i.e.*, adopting in whole and without any scrutiny the clearly unsupported and unsupportable assertions of the Russian Federal Tax Service). During the course of the appeals process, the Yukos receiver commenced meritless and unsupported proceedings to invalidate the Loans (flatly inconsistent with the Tax Service's position

that the Loans had already been invalidated) in order to delay the appeals while the receiver hastened to conclude the bankruptcy.

30. Thus, irrespective of the illegal dismantling of Yukos Oil and in the alternative, the arbitrary and capricious denial of Yukos Capital's right to participate as a creditor in the Yukos bankruptcy constituted an expropriation of its investments (*i.e.*, the Loans) as there was no other recourse available. In addition, creditors similarly situated to Yukos Capital (*e.g.*, other Yukos subsidiaries acquired by Rosneft in the sham auctions) had their claims against Yukos recognised in the bankruptcy and paid. This unfair and discriminatory treatment further acted to deprive Yukos Capital of the value of its investment.

31. By letter dated 23 May 2008, Yukos Capital notified the Russian Federation, through the Russian Ministry of Justice, of its claims under the ECT, accepted the Russian Federation's offer to arbitrate and invited the Russian Federation to engage in settlement discussions. On 22 August 2008, counsel to Yukos Capital received the notice back from the Ministry of Justice with a note that receipt of such notices was not within the Ministry's competence. By letter dated 27 August 2008, Yukos Capital's 23 May 2008 Notice was forwarded to the Government of the Russian Federation and the Administration of the President of the Russian Federation.[12]

V. THE ENERGY CHARTER TREATY

32. The ECT is a multi-lateral treaty created with the goal of liberalising investment and trade in energy. It includes provisions designed to ensure the opening up of the energy sector, including non-discriminatory treatment of investors, free transit of energy products, transfer of capital and returns, and measures aimed at eliminating anti-competitive practices. The ECT grants investors of State parties the right to bring legal proceedings, including international arbitration, against all other State parties for breach of the ECT's provisions relating to investment promotion and protection.

33. The ECT was signed on 17 December 1994 and entered into force on 16 April 1998. The Russian Federation signed the ECT on 17 December 1994. The ECT applied provisionally to Russia until 19 October 2009, sixty days after it provided notice to

---

12 A copy of the 27 August 2008 letter and attachments is annexed hereto as Exhibit C103.

the Portuguese Republic, as Depository of the ECT, of its intention not to become a party to the Treaty pursuant to Article 45(3)(a) thereof.

34. Part III of the ECT is titled "Investment Promotion and Protection" and includes the ECT's substantive protections for investment in energy. Among other things, Part III, Article 10(1) obligates Contracting Parties to "*create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area.*" Article 10(1) continues:

> "*Such conditions shall include a commitment to accord at all times to Investments of Investors of other Contracting Parties fair and equitable treatment. Such Investments shall also enjoy the most constant protection and security and no Contracting Party shall in any way impair by unreasonable or discriminatory measures their management, maintenance, use, enjoyment or disposal. In no case shall such Investments be accorded treatment less favourable than that required by international law, including treaty obligations. Each Contracting Party shall observe any obligations it has entered into with an Investor or an Investment of an Investor of any other Contracting Party.*"

35. In Article 10(7), Contracting Parties are further obligated to:

> "*Accord to Investments in its Area of Investors of other Contracting Parties, and their related activities including management, maintenance, use, enjoyment or disposal, treatment no less favourable than that which it accords to Investments of its own Investors or of the Investors of any other Contracting Party or any third state ...*"

36. Completing Article 10, Article 10(12) provides that "[*e*]*ach Contracting Party shall ensure that its domestic law provides effective means for the assertion of claims and the enforcement of rights with respect to Investments, investment agreements, and investment authorizations.*"

37. Part III, Article 13, provides that investments may not be "*nationalized, expropriated or subjected to a measure or measures having effect equivalent to nationalization or expropriation*" except where it is in the public interest, not discriminatory, carried out under due process of law and accompanied by the payment of "*prompt, adequate and effective compensation.*" Such compensation is to equate to the "*fair market value of the Investment expropriated at the time immediately before the Expropriation or impending Expropriation became known ....*"

38. The resolution of disputes arising under the ECT is addressed in Part V, Article 26, addressing investor-state disputes. As set forth in Article 26(1), the ECT investor-state dispute resolution provisions apply to:

> *"Disputes between a Contracting Party and an Investor of another Contracting Party relating to an Investment of the latter in the Area of the former, which concern an alleged breach of an obligation of the former under Part III ..."*

39. Disputes concerning alleged breaches of obligations under ECT Part III must, if possible, be settled amicably. If such disputes are not settled within three months from a request for amicable settlement, the Investor party to the dispute may choose to submit it for resolution (i) to the courts of the Contracting Party to the dispute, (ii) in accordance with any previously agreed dispute settlement procedure, or (iii) in accordance with the international arbitration provisions of the ECT. Pursuant to ECT Article 26(4), arbitration under the UNCITRAL Rules is specified as an option open to investors.

VI. THE TRIBUNAL'S JURISDICTION

40. As applicable to this proceeding, the jurisdictional requirements for arbitration under the ECT are that (i) Yukos Capital is an Investor, (ii) Russia is a Contracting Party, (iii) the dispute relates to an Investment by Yukos Capital in Russia and (iv) the dispute concerns an alleged breach of Russia's obligations contained in Part III of the ECT. Each of these requirements is met.

A. Yukos Capital is an Investor

41. In relevant part, "*Investor*" is defined in Article 1(7) of the ECT as, with respect to a Contracting Party, "*a company or other organization organized in accordance with the law applicable in that Contracting Party.*"

42. Luxembourg is a Contracting Party to the ECT, having signed the ECT on 17 December 1994, ratified it on 7 February 1997 and deposited its instrument of ratification on 27 November 1997. Yukos Capital is a company organised in

accordance with the law applicable in Luxembourg.[13] Accordingly, Yukos Capital is an Investor.

B. Russia is a Contracting Party for Purposes of this Proceeding

43. Russia signed, but did not ratify, the ECT. The application of the ECT to signatories in Russia's former position is addressed in Part VIII, Article 45, headed "*Provisional Application.*" ECT Article 45 provides in pertinent part as follows:

> *"(1) Each signatory state agrees to apply this Treaty provisionally pending its entry into force for such signatory in accordance with Article 44, to the extent that such provisional application is not inconsistent with its constitution, laws or regulations.*
>
> *(2) (a) Notwithstanding paragraph (1) any signatory may, when signing, deliver to the Depository a declaration that it is not able to accept provisional application. The obligation contained in paragraph (1) shall not apply to a signatory making such a declaration ...*
>
> * * *
>
> *(3) (a) Any signatory may terminate its provisional application of this Treaty by written notification to the Depository of its intention not to become a Contracting Party to the Treaty. Termination of provisional application for any signatory shall take effect upon the expiration of 60 days from the date on which such signatory's written notification is received by the Depository.*
>
> *(b) In the event that a signatory terminates provisional application under subparagraph (a), the obligation of the signatory under paragraph (1) to apply Parts III and V with respect to any Investments made in its Area during such provisional application by Investors of other signatories shall nevertheless remain in effect with respect to those Investments for twenty years following the effective date of termination, except as otherwise provided in subparagraph (c).*
>
> *(c) Subparagraph (b) shall not apply to any signatory listed in Annex PA ..."*

44. ECT Article 45(3)(a) provides that: "*Termination of provisional application for any signatory shall take effect upon the expiration of 60 days from the date on which such*

---

[13] Exhibit C117.

signatory's written notification is received by the Depository." As noted previously, Russia provided notice pursuant to Article 45(3) on 20 August 2009, thus terminating provisional application of the ECT as of 19 October 2009. Prior to that time, the whole of the ECT applied to the Russian Federation.

45. Furthermore, pursuant to Article 45(3)(b) of the ECT, investment-related obligations, including the obligation to arbitrate investment-related disputes under Part V of the ECT, remain in force for a period of 20 years following the effective date of termination of provisional application. In the case of the Russian Federation, this means that any investments made in Russia prior to 19 October 2009, including Yukos Capital's investments, continue to benefit from the ECT's protections for a period of 20 years—*i.e.*, until 19 October 2029. Russia therefore remains obligated to apply ECT Parts III (the substantive protections) and V (dispute resolution) to Yukos Capital's investments.

46. Further, nothing about provisional application of the ECT is inconsistent, or can even be said to be inconsistent, with the Russian Federation's constitution, laws or regulations. Russia did not, upon signing, deliver a declaration that it was unable to accept provisional application of the ECT and Russia is not listed in Annex PA to the ECT.

C. <u>The Dispute Relates to Investments Made by Yukos Capital in Russia</u>

47. "*Investment*" is defined in Article 1(6) of the ECT:

> *"'Investment' means every kind of asset, owned or controlled directly or indirectly by an Investor and includes:*
>
> > *(a) tangible and intangible, and movable and immovable, property, and any property rights such as leases, mortgages, liens, and pledges;*
> >
> > *(b) a company or business enterprise, or shares, stock, or other forms of equity participation in a company or business enterprise, and bonds and other debt of a company or business enterprise;*
> >
> > *(c) claims to money and claims to performance pursuant to contract having an economic value and associated with an Investment;*
> >
> > *(d) Intellectual Property;*
> >
> > *(e) Returns;*

> *(f) any right conferred by law or contract or by virtue of any licenses and permits granted pursuant to law to undertake any Economic Activity in the Energy Sector."*

48. The Loans made by Yukos Capital to Yukos Oil, intended initially to help finance a major acquisition in Russia and later to assist in the survival of an enterprise making substantial contributions to the Russian economy in an industry of strategic importance, are (i) assets of Yukos Capital's, (ii) debts of Yukos Oil's and (iii) claims to money. There can be no question that the Loans constitute Investments under the ECT.

D. <u>The Dispute Concerns Alleged Breaches of Russia's ECT Obligations</u>

49. As outlined above and as will be developed more fully below and during the course of this proceeding, Yukos Capital alleges that acts attributable to the Russian Federation expropriated its Investments (both directly and indirectly) and, in so doing, breached numerous obligations under Part III of the ECT, including Russia's obligations:

- to provide fair and equitable treatment (Art. 10(1);
- to provide constant protection and security (Art. 10(1);
- not to impair the use, enjoyment or disposal of an investment by unreasonable or discriminatory measures (Art. 10(1);
- not to accord treatment less favourable than that required under international law (Art. 10(1);
- not to accord treatment less favourable than that accorded to other investors (Art. 10(7);
- to provide effective means for the assertion of claims and the enforcement of rights (Art. 10(12); and
- not to expropriate investments or subject them to measures having an effect equivalent to expropriation (Art. 13(1).

VII. THE EXPROPRIATION OF YUKOS CAPITAL'S INVESTMENTS

A. <u>The Dismantling and Destruction of Yukos Oil</u>

50. With the collapse of the Soviet Union in 1991, Russia inherited huge state-owned industries run by ineffective "red managers" resistant to modernisation and plagued by corruption and organised crime.

51. Due to mismanagement and underinvestment, the infrastructure of Yukos Oil Company was crumbling and its wells produced a fraction of their peak capacity at inflated costs. In 1996, Mikhail Khodorkovsky and his business partners invested in a

majority stake in Yukos when the company was put up for privatisation under the Yeltsin administration's "loans for shares" programme. At the time, Yukos was producing just half a million barrels of oil per day, compared to 1.4 million in 1987, at a cost of up to USD 12 per barrel. It also had between USD 2-3 billion in debt.

52. With his partners, Khodorkovsky implemented an historic turnaround. In the span of a few years, they reduced per barrel costs to USD 1.5 and increased production to over one million barrels per day. By 2003, Yukos and its subsidiaries produced 20 per cent of Russia's oil – the equivalent of 2 per cent of world production. The company had become the second-largest taxpayer in Russia after the state gas monolith, Gazprom, contributing 4.1 per cent of the Russian federal budget. In 2002, Vedomosti, Russia's leading business daily, jointly published by the Financial Times and the Wall Street Journal, awarded Khodorkovsky its annual "Entrepreneur of the Year" prize.

53. In 2001, Yukos issued depositary receipts in regard to up to 20% of its shares. In the years 1996-2003, the Yukos group experienced considerable growth, becoming owner of substantial oil and gas reserves, pipelines and refineries (both in Russia and internationally). Yukos was subject to SEC regulation, its annual reports and accounts were prepared by PricewaterhouseCoopers ("PwC") and Yukos was the only large Russian company to comply with American accountancy standards (*i.e.*, US GAAP). Yukos achieved in all respects a transparency unprecedented in Russia.

54. As the Russian journalist Anna Politkovskaya-who was murdered in October 2006– wrote in "*Putin's Russia,*" Yukos was:

> *"the most transparent company in our corrupt country, the first to function in accordance with internationally accepted financial practice. It operated 'in the white' as people say in Russia, and what is more it donated over 5 per cent of its gross annual profit to financing a large university, children's homes and an extensive programme of charitable work."*[14]

[14] Anna Politkovskaya, Putin's Russia, UK: Harvill, 2004, p. 276 (Exhibit C11).

55. In the spring of 2003, Yukos Oil Company was valued at approximately USD 70 billion[15] and its market capitalisation was in excess of USD 40 billion. Khodorkovsky, the indirect majority shareholder and CEO, was one of the most successful entrepreneurs in Russia (but also a contributor to the country's democratic opposition). In April 2003, Yukos and Sibneft, indirectly majority owned by Roman Abramovich, announced their planned merger. Khodorkovsky was to head the new company, YukosSibneft, estimated to have annual crude oil production in excess of 100 million tons. At around the same time, Khodorkovsky held talks with ChevronTexaco and ExxonMobil on the possibility of their purchase of interests in the company or even a full business combination.

(i) <u>The Politically Motivated Attacks Begin</u>

56. As noted, Khodorkovsky had taken steps to transform Yukos along the lines of western business models. These steps included the introduction of corporate transparency, the adoption of western accounting standards, the hiring of western management, the creation of an independent board of directors with a corporate governance subcommittee, corporate growth through mergers and acquisitions, and increased western investments. These actions marked Khodorkovsky as an outspoken leader who was pro-western and challenged the non-transparent means by which government and business operated in the Russian energy sector. All of this deeply unsettled the Kremlin.

57. In 2002 and 2003, Khodorkovsky became increasingly outspoken on Russia's rampant corruption and on the need to create a more robust civil society. In February 2003, in a televised meeting between President Putin and the Russian Union of Industrialists and Entrepreneurs, Khodorkovsky cited numerous statistics on state graft in Russia showing that corruption cost the Russian economy over USD 30 billion per year. He said the Putin administration "*must be willing to show its readiness to get rid of some odious figures*" in the regime, to prove its readiness and ability to combat corruption. An angry President Putin shot back with clear threats to

---

15 As derived from negotiations with ExxonMobil concerning the potential acquisition of a 25% stake in Yukos at a price of USD 17.5 billion.

Khodorkovsky and questioned the legitimacy of Yukos' growth.[16] A more programmed and forceful retaliation was soon to follow.

58. On 2 July 2003, Platon Lebedev, a close associate of Khodorkovsky's and Chairman of the Board of Group Menatep, was arrested whilst in hospital and detained, ostensibly on suspicion of theft of shares in a company known as Apatit. Two days later, Khodorkovsky and Leonid Nevzlin, holder of a substantial interest in Group Menatep, were called in for questioning by the Russian Prosecutor General. A series of searches and seizures, often conducted by armed SWAT teams, were conducted at the offices of Yukos and its affiliates. Criminal proceedings were instituted against persons linked with Yukos and its directors and, on 25 October 2003, Khodorkovsky was arrested at gun point, charged and later convicted after a trial characterised by a shocking lack of due process. Lebedev suffered the same fate.

59. The motive behind the Russian State's attacks against persons associated with Yukos cannot be disputed. As summarised in European Parliamentary Assembly Resolution 1418 (2005),[17] adopted following an extensive investigation headed by Mrs. Leutheusser-Schnarrenberger, former Federal Minister of Justice of Germany:

- *"Facts pointing to serious procedural violations committed by different law-enforcement agencies against Mr. Khodorkovsky, Mr. Lebedev and Mr. Pichugin, former leading Yukos executives, have been corroborated during fact-finding visits ... On the whole, the findings call into question the fairness, impartiality and objectivity of the authorities, which appear to have acted excessively in disregard of fundamental rights of the defence ..."*

- *"The Assembly notes that the circumstances surrounding the arrest and prosecution of the leading Yukos executives strongly suggest that they are a clear case of non-conformity with the rule of law and that these executives were – in violation of the principle of equality before the law – arbitrarily singled out by the authorities."*

- *"Intimidating action by different law-enforcement agencies against Yukos and its business partners and other institutions linked to Mr. Khodorkovsky and his associates and the careful preparation of this action in terms of public relations, taken together, give a picture of a coordinated attack by the state."*

---

16 Vanity Fair, *The Wrath of Putin* (April 2012), p. 5 (Exhibit C115).

17 European Parliament Resolution 1418, *The circumstances surrounding the arrest and prosecution of leading Yukos executives* (25 January 2005), ¶¶ 7, 9. 11 and 14 (Exhibit C54).

- *"[T]he Assembly considers that the circumstances of the arrest and prosecution of leading Yukos executives suggest that the interest of the state's action in these cases goes beyond the mere pursuit of criminal justice, and includes elements such as the weakening of an outspoken political opponent, the intimidation of other wealthy individuals and the regaining of control of strategic assets."*

60. Other neutral institutions have come to similar conclusions. For example, in a judgment of 18 March 2005,[18] the English Magistrates' Court refused to extradite two Yukos Oil employees, Dmitri Maruev and Natalya Chernysheva. In its judgment, the court found, among other things (page 4):

> *"In view of the facts that I have outlined I am satisfied that it is more likely than not that the Prosecution of Mr Khodorkovsky is politically motivated. As the allegation against these defendants is on the basis of a conspiracy with Mr Khodorkovsky, in my view it is the inevitable conclusion that the Prosecution of these two defendants is also politically motivated."*

61. In another extradition case, the Supreme Administrative Court of Lithuania determined, in a judgment dated 16 October 2006,[19] that:

> *"(T)he panel of judges states that the data collected in the materials of the request for asylum will no doubt prove that the so-called 'OC Yukos (Mikhail Khodorkovsky's)' trial in the Russian Federation was politicised, i.e., the circumstances of the criminal prosecution suggest that the interest of the State's action in these cases goes beyond the mere pursuit of criminal justice, to include such elements as to weaken an outspoken political opponent and to regain control of strategic economic assets. Moreover, the official public authorities treated the persons under criminal prosecution in that particular case in a discriminatory way, i.e., worse than other persons against whom criminal charges were brought for analogous crimes. This undoubtedly means that there are grounds for the persons attributed by the official Russian authorities to the 'OC Yukos (Mikhail Khodorkovsky's) trial' to feel fear of prosecution in the Russian Federation."*

62. In a judgment issued by the English City of Westminster Magistrates' Court dated 19 December 2007,[20] when asked to consider yet another extradition request, the court concluded:

---

[18] *Government of the Russian Federation v. Dmitry Maruev and Natalya Chernysheva*, Bow Street Magistrates' Court, Tim Workman, Senior District Judge (18 March 2005) (Exhibit C55).

[19] Supreme Administrative Court of Lithuania, Administrative Case No. A – 2193/06 (16 October 2006), page 20, (Exhibit C79).

> *"This request is linked to the events surrounding the notorious cases involving NK Yukos and Mikhail Khodorkovsky. That there is a 'reasonable chance' or 'reasonable grounds for thinking' or a 'serious possibility' that this prosecution is being pursued for a collateral purpose because of the defendant's imputed political opinions. (...) There is, in my mind, a strong suspicion that the prosecution is being brought for political and economic reasons. For those reasons I find the defendant would be prejudiced at any trial in the RF. Given the high profile of this case, and on the basis of the defence evidence, I am not confident that a fair trial will be possible. The uncontested expert evidence suggests the judiciary in a case such as this will be pressured to support the prosecution. The evidence suggests the judiciary lacks independence; the surprisingly low acquittal rates, and the requirement on judges to 'justify' acquittals, is worrying."*

63. Similarly, the English Court of Appeal more recently reflected on the Yukos case as a telling example of government interference:

> *"The three instances of government interference in the judicial process on which the judge relied are the proceedings relating to Yukos, Films by Jove and Media Most. It can be said with some justification that the Yukos case involved both what might be described as the re-nationalisation of strategic assets and the damaging of a political opponent."*[21] *(emphasis added)*

64. The Tribunal Fédéral Suisse, the highest court of Switzerland, for the first time in history refused a Russian request for the transmission of documents, again in connection with Yukos (judgment dated 13 August 2007):[22]

> *"L'ensemble de ces éléments corrobore clairement le soupçon selon lequel la procédure pénale serait en l'occurrence instrumentalisée par le pouvoir en place, dans le but de mettre au passe la classe des riches 'olicharges' et d'écarter des adversaires politiques potentiels ou déclarés."*[23]

[Footnote continued from previous page]

20 *The Government of the Russian Federation v. Andei Borisovich Azarow*, City of Westminster Magistrates' Court, Judge N. Evans (19 December 2007), ¶ 15 (Exhibit C98).

21 *Deripaska v. Cherney* [2009] EWCA Civ 849, ¶ 66 (Exhibit C106).

22 *Mikhail Khordorkovski v. The Office of the Attorney General of the Swiss Federation*, 1A.29/2007/col, Judgment of Tribunal Fédéral Suisse (13 August 2007) (Exhibit C92).

23 *"All of the evidence clearly corroborates the suspicion according to which the criminal proceeding would be, in the case in question, manipulated by the power in place, with the aim of putting the class of rich 'oligarchs' in step and moving away from potential or declared political adversaries."*

65. In January 2011, the Lithuanian authorities again denied the Russian Federation's extradition requests, this time in connection with the extradition of Vladimir Dubov.[24] The request was denied on the basis that:

> *"It is evident [...] that the charges made by the Russian Federation against shareholders and executives of NK Yukos have certainly been made seeking to prosecute and punish them for their political opinions. It thus follows that Vladimir Dubov is prosecuted for his belonging to a social group associated with Michail Khodorkovsky and characterized by common, permanent, invariable features (a group of persons in the NK Yukos case), which is prosecuted by the Russian Federation. It is therefore very likely that prosecution of Vladimir Dubov is politically motivated and the request for extradition is made for the purpose of prosecuting or punishing him for his political opinions. Furthermore, reasonable doubts arise that Vladimir Dubov's criminal trial in the Russian Federation will be fair and impartial, i.e. that his rights to a fair trial will not be prejudiced."*[25]

66. Despite being convicted and sentenced to nine years in prison (reduced to eight on appeal), the persecution of Khodorkovsky and Lebedev has continued. In February 2007, new charges of embezzlement and money laundering were leveled against them and just one year before their initial sentences were set to expire (27 December 2010), they were convicted and sentenced to fourteen years imprisonment in circumstances plagued by due process violations. Many trial observers, such as representatives from the International Bar Association and Amnesty International, have observed that the trial was not fair and "*[t]he continuing disregard for due process and the consistent attempts to obstruct the preparation of the defence has only strengthened the impression that the current conviction of Mikhail Khodorkovsky and Platon Lebedev has been sought, and for now, achieved, for political ends and without consideration for the most elementary requirements of justice.*"[26]

---

24 A member of the Board of Directors of Yukos Oil Company from 1998 to 1999, State Duma Deputy and Chairman of the Tax Sub-Committee of the State Duma from 2000 to October 2003, and a beneficiary of trusts holding shares in GML Limited.

25 *Decision to Deny Extradition of Vladimir Dubov to the Russian Federation*, Prosecutor General's Office of the Republic of Lithuania, 28 January 2011, p. 9 (the decision was approved by the Vilnius Regional Court) (Exhibit C112).

26 Amnesty International, Public Statement of 27 December 2010, *Unfair trial concerns cast doubt on the integrity of the conviction of Mikhail Khodorkovsky and Platon Lebedev*, page 4 (Exhibit C110).

67. The European Parliament issued a further resolution on 9 June 2011, following the Moscow City Court Appeal in relation to Khodorkovsky's and Lebedev's convictions, underlining the politically motivated character of the trial:

> *"[The European Parliament] [t]akes note with concern of the ruling handed down by the Russian appeal court against Mikhail Khodorkovsky and his business associate Platon Lebedev on 26 May 2011 as a continuation of politically motivated court decisions; condemns political interference with the trial; welcomes President Medvedev's decision to examine this case in the Presidential Human Rights Council; welcomes the European Court of Human Rights' ruling in this case accepting Khodorkovsky's claims of unlawful detention..."*[27]

68. As noted in the resolution, the Former Russian President, Dmitry Medvedev, requested that his own Human Rights Council, a consultative body established to assist the President in the exercise of his constitutional responsibilities to guarantee and protect human rights and freedoms, conduct a public examination into the most recent criminal cases against Khodorkovsky and Lebedev. In December 2011, the Human Rights Council issued a damning report, concluding that the verdicts were unsafe and unjust and violated the defendants' human rights.[28]

(ii) <u>The Attack Expands to Yukos</u>

69. The Russian State assault on Khodorkovsky and individuals associated with Yukos was accompanied by an equally vicious assault on Yukos itself which, ultimately, acted to expropriate Yukos Capital's Investment. The assault on Yukos used as its vehicle a series of purported tax re-assessments and related enforcement proceedings.

(a) <u>The Tax Re-Assessments</u>

70. The tax story starts with an extensive audit conducted by the Russian tax authorities in 2002-2003 (before the attacks on Khodorkovsky began). In late 2002, a tax inspection, or audit, of Yukos was ordered by the regional tax authorities where Yukos was incorporated (*i.e.*, Nefteyugansk). The audit covered the 2000 and 2001

---

27 European Parliament resolution of 9 June 2011 on the EU-Russia summit, ¶ 16 (Exhibit C113).

28 Report of the Presidential Council of the Russian Federation for the Development of Civil Society and Human Rights on the results of the public scholarly analysis of the court materials of the criminal case against M. B. Khodorkovsky and P. L. Lebedev (Moscow, 2011) (Exhibit C111).

tax years and was conducted from October 2002 through March 2003. A detailed report of the audit was prepared and served on Yukos in April 2003.[29]

71. Yukos lodged certain objections to the audit report, following which the Nefteyugansk Tax Office adopted Resolution 289 finding that Yukos had failed to make complete returns in respect of three types of tax: profit tax, value added tax and oil excise duty.[30] In monetary terms, Resolution 289 required that Yukos make an additional tax payment of RUR 8,956,048.04 (approximately USD 290,000)[31] for 2000 and 2001. This additional assessment was promptly paid and the tax authorities issued certificates on 19 September 2003, 23 October 2003 and 17 November 2003 confirming that: (i) Yukos Oil had no tax debts outstanding for the years 2000 and 2001 and (ii) the company had not committed any tax offences.[32]

72. Approximately one month later, on 8 December 2003 (and with the orders to crush Yukos having been issued), the Russian Tax Ministry served notice that a further tax audit would be carried out for the 2000 tax year. Unlike the first audit, which had gone on for months and resulted in the report of 28 April 2003, the "re-audit" took a mere ten days. On 29 December 2003, a new report was issued by the Tax Ministry in which Yukos Oil Company was assessed to have underpaid 2000 taxes by RUR 79.6 billion (USD 2.72 billion), which along with fines and penalty interest came to a tax debt of RUR 98.5 billion (USD 3.37 billion).[33]

73. In reliance on the 29 December 2003 report, the tax authorities issued Resolution #14-3-05/1609-1 on 14 April 2004 (the "*2000 Tax Assessment*").[34] The 2000 Tax Assessment asserted against Yukos an additional liability to tax, penalty interest and

---

29 Field Tax Audit Report No. 66 of OAO Yukos Oil Company of 28 April 2003 (Exhibit C4).

30 Decision No. 289 of 9 June 2003 to hold OAO Yukos Oil Company Liable for a Tax Offence (Exhibit C5).

31 Based on a RUR/USD exchange rate of 31.1000/1 as reported by the Central Bank of Russia on 28 April 2003.

32 Certificates No. 47-10-11/994/1 of 19 September 2003 (Exhibit C6), No. 47-10-11/1612 of 23 October 2003 (Exhibit C7), and No. 47-10-11/1908 of 17 November 2003 (Exhibit C8).

33 Field Tax Audit Report No. 08-1/1 of OAO Yukos Oil Company of 29 December 2003 (Exhibit C10);based on a RUR/USD exchange rate of 29.2533/1 as reported by the Central Bank of Russia on 29 December 2003.

34 Resolution No. 14-3-05/1609-1 to Hold the Taxpayer Fiscally Liable for a Tax Offence (14 April 2004) (Exhibit C13).

fines for the year 2000 of RUR 99.4 billion (approximately USD 3.48 billion).[35] As set forth in the 2000 Tax Assessment, the theory on which this additional liability was asserted is the following:

> *"The field tax audit [i.e., the 're-audit'] showed that OAO NK YUKOS did not reflect the receipts from the sales of products (work, services) as a result of using an illegal tax evasion scheme by means of artificially founding fake organizations in the oil and after-product movement chain and registering them in territories with preferential tax treatment.*
>
> *The scheme was aimed at non-payment of profit tax, value-added tax, motorway user tax, tax on the sales of petroleum, oils and lubricants ('POL') and housing stock and social amenities maintenance tax on the amount of receipts (income) from oil and after-product sales. For this purpose OAO NK YUKOS created fake dependent organizations to be oil and after-product owners (hereinafter referred to as 'owners'). These organizations were registered in territories with preferential tax treatment (closed administrative and territorial formations, Russian Federation constituent entities giving tax preferences on investments). OAO NK YUKOS retained control over the oil and after-product operations performed by the 'owners' by means of participating in the deals as mediator itself or involving its other dependent organizations to act as mediators in the deals.*
>
> * * *
>
> *As a result of this oil and after-product sales illusion the sales revenues (income) belonged to the mentioned fake organizations. Thus, as per their records, it was the 'owners' who registered tax obligations. At the same time, as these organizations illegally used tax preferences, the budget did not receive the related profit tax, motorway user tax, property tax and housing stock and social amenities maintenance tax.*
>
> *The audit found, that the true owner of the oil and after-products was OAO NK YUKOS. It was OAO NK YUKOS, which purchased the oil, transferred it for processing and sold the oil and after-products, and this is to be proved by the actual oil and after-products movement from the producers to the refineries or to the oil tank farms related to OAO NK YUKOS (supported by transportation documents), as well as by the fact of OAO NK YUKOS direct participation in all the deals ..."*[36]

---

35 Based on a RUR/USD exchange rate of 28.5892/1 as reported by the Central Bank of Russia on 14 April 2004.

36 Field Tax Audit Report No. 08-1/1 of OAO Yukos Oil Company of 29 December 2003, pp. 10-12 (Exhibit C10)

74. The 2000 Assessment was just the first in a series of massive "re-assessments." Between 2004 and 2006, the Russian tax authorities re-assessed Yukos for approximately RUR 692 billion (USD 24 billion) of additional tax liabilities in respect of the 2001-2004 tax years, all on the basis of the same "theories" propounded in the 2000 Tax Assessment. As discussed below, the tax re-assessments were entirely without basis and the linchpin to a politically motivated scheme to single out and destroy Yukos. Yukos' subsidiaries were also faced with large tax reassessment claims for the years 2001-2003.

75. During the relevant period, Yukos itself carried out no oil production, refining, trade or retail operations, but held shares in numerous subsidiary companies that performed these various tasks. This holding structure employed by the Yukos group was and is common practice for oil company groups in Russia, including Lukoil, Sibneft (now GazpromNeft), TNK-BP, Surgutneftegaz and, prior to 1 October 2006, Rosneft Oil Company.

76. Each of the Yukos group companies, including Yukos, paid the applicable taxes on their own turnover and profits on an individual basis as required by Articles 19 and 45(1) of the Tax Code of the Russian Federation (the "*Tax Code*").

77. Approximately 95% of the tax liabilities re-assessed to Yukos were actually liabilities the Tax Ministry calculated in respect of other companies and then assigned to Yukos. Some of those companies were Yukos subsidiaries. Others were not. The justification put forward by the Tax Ministry for its approach was that the Yukos group exported oil through various trading companies (the "*trading companies*") registered in regions with favourable tax rates ("*special investment zones*"). The Tax Ministry alleged that this amounted to unlawful tax avoidance because the use of trading companies registered in special investment zones served no viable economic purpose other than the reduction of tax.[37]

78. The fundamental flaw of this approach is that there is no provision of Russian law allowing the Tax Ministry to "pierce the corporate veil" and assign the tax liabilities of one company to another, even if it is a subsidiary, dependent or affiliate entity or

---

[37] *See, e.g.*, Decision no. 30-3-15/3 on Holding a Taxpayer Liable for Tax Offences (2 September 2004) p. 20 (Exhibit C32).

none of the above. To the contrary, at all relevant times reduction of a company's tax burden in this way (*i.e.*, tax optimisation) was not prohibited, but promoted by Russian law. Russian legal culture relied on strict formal rules and had no concept of legally compliant but "abusive" tax schemes. A tax reduction or optimisation scheme either complied with the formal rules or it did not. Moreover, the special investment zones were not offshore jurisdictions competing with Russia for tax revenue. The relevant federal tax legislation expressly allowed the special investment zones to determine their own tax rates and the rules for claiming them, a policy tool that positively encouraged tax competition within Russia. Nor is there any provision for consolidated tax assessment of company groups or centralised collection of a group's aggregate tax liabilities from a parent or holding company. Each individual company is required to declare and pay its own individual taxes.

79. Mikhail Kasyanov, the Prime Minister of the Russian Federation from 2000-2004, the precise period for which Yukos' tax practices were singled out for penalties, has described the situation as follows:

> "*Well, during this period, uniform treatment existed for all companies, and the major oil companies enjoyed basically the same treatment. Really, the principal traits consisted of the vertical integration of these major companies, second – the use of transfer pricing, and third – availing themselves of the so-called low-tax regions permitted by law; almost...not almost, but rather all these companies shared those traits, which were inherent in these nine companies and others. I am talking about the nine, since I met regularly, well, regularly, perhaps once every six months, with the heads of these major companies, the largest oil companies.*"[38]

80. In an interview in January 2004, Mr Kasyanov was asked to comment on the Tax Ministry's retroactive application to Yukos of new theories declaring such tax optimisation regimes to be unlawful. He gave the following striking answer:

> "'*If legal tax optimization activity is declared illegal retroactively, then I view this negatively. For the simple reason that the law had holes that allowed for optimization payments. The Tax Code did not*

38 Transcript of testimony of M. Kasyanov, 24 May 2010, Khamovnichesky Court of Moscow, Second Trial of Mikhail Khodorkovsky, p.3 (Exhibit C108).

> *prohibit Yukos and other companies to conduct transactions through internal offshores.* '"[39]

81. Mr Kasyanov addressed the issue even more bluntly in another interview: when asked "[*So,*] *it turns out that everything that Khodorkovsky and the other Yukos shareholders were blamed for was the norm until 2003?*", he stated: "*With regard to tax obligations - yes. Optimization of tax payments through domestic offshore zones was completely legal based on legislation at the time.*"[40]

82. In addition, the tax liabilities "re-assessed" against Yukos were in respect of economic operations that had been reported by the Yukos group companies in their own respective tax declarations. The local tax inspectorate was aware of the trading companies due to Yukos Oil's own declared business dealings with them.

83. Moreover, Yukos' tax structure was widely known through the public disclosures it made, including in its financial statements. For example, Yukos' US GAAP 2001 Consolidated Financial Statements disclosed the following:

> "*During 2001 and 2000, our effective tax rate was 18% and 24%, respectively, which was significantly less than the maximum statutory rates during those years. Our subsidiaries operate in several tax jurisdictions both within Russia and internationally. Many of our subsidiaries are resident in tax jurisdictions in Russia where statutory tax rates are lower or where we benefit from regional tax incentives. In addition several other factors have had a significant impact in reducing our effective tax rate during these years, including the investment tax credits.*"[41]

84. Since the Yukos group companies (including the trading companies) had disclosed their operations to the Tax Ministry, Yukos had carried out its business with the legitimate expectation that it owed no outstanding tax liabilities. This expectation was confirmed by the series of tax certificates issued in late 2003.

---

39 Alexander Bekker, Vladimir Fedorin, 'Interview: Mikhail Kasyanov, Prime Minister of the Russian Federation', *Vedomosti*, 12 January 2004, p. 9 (Exhibit C12).

40 Mikhail Kasyanov, 'Without Putin: Political Dialogues with Evgeny Kiselev', Novaya Gazeta, Moscow, 2009, p.196 (Exhibit C104).

41 Yukos Management's Discussion and Analysis, 31 December 2001, p. 11 (Exhibit C2).

85. Indeed, as the European Parliamentary Assembly reflected in its Resolution 1418 (2005):[42]

> *"In particular, the allegedly abusive practices used by Yukos to minimize taxes were also used by other oil and natural resource companies operating in the Russian Federation, which have not been subjected to a similar tax reassessment, or its forced execution, and whose leading executives have not been criminally prosecuted. Whilst the law was changed in 2004 and the alleged 'loophole' thus closed, the incriminated acts date back to 2000 and retrospective prosecution started in 2003.*
>
> * * *
>
> *Making criminal charges against persons who made use of the possibilities offered by the law as it stood at the time of the incriminated acts, following a retroactive change of the tax law, raises serious issues ...."*

86. A report prepared by Mrs. Leutheusser-Schnarrenberger, Special Rapporteur to the Council of Europe, in connection with the Assembly's investigation contains the following:

> *"As to the reproach of discriminatory treatment, I had an interesting exchange of views during my first visit at the [Russian] State Duma with a representative of the tax ministry. He described to me the 'abusive' techniques used by Yukos to minimise taxes by letting part of the profits of the mother company accrue to dependent companies domiciled in inner-Russian tax havens. He confirmed that in 2000 (the year for which the first tax reassessment – RRoub 99 bn/USD 3.3 bn – is levelled against Yukos), these techniques were widely used and considered 'legal', albeit anti-social in the case of large companies not contributing to any real economic development of the tax haven regions. The law making such 'abuses' possible has therefore been changed ... [and] entered into force only in 2004."*[43]

87. Mrs. Leutheusser-Schnarrenberger's report addendum notes that in response to her written requests to the Russian tax authorities for "*official figures on the comparative tax burden for oil producing companies, the reply was evasive.*" This evasiveness provided further support (although none was needed) for her conclusion that "*Yukos*

---

42 European Parliament Resolution 1418, *The circumstances surrounding the arrest and prosecution of leading Yukos executives* (25 January 2005), ¶¶ 10 and 12 (Exhibit C54).

43 Report of Committee on Legal Affairs and Human Rights by Rapporteur: Mrs. Sabine Leutheusser-Schnarrenberger, *The circumstances surrounding the arrest and prosecution of leading Yukos executives*, Doc. 10368 (29 November 2004), ¶ 66 (Exhibit C39).

and its leading executives have indeed been 'arbitrarily singled out by the authorities'..."[44]

88. In another report prepared in August 2009, the Special Rapporteur similarly concluded that: "*no other oil industry executive in the Russian Federation has been accused of embezzling all the oil produced by his company and laundering the proceeds of the sale for having made use of the same vertically-integrated business structure that is the standard of the industry...*"[45]

89. The more recent revisionist "justifications" offered by the Respondent, that it was entitled to single out Yukos because it was allegedly engaged in "sham" transactions or motivated by "bad faith," are specious and have no basis in Russian law or practice during the relevant period. The Tribunal in *Quasar De Valores* found as follows with respect to the sham transaction suggestion:

> "*In the present case, there was nothing of the sort. The sales transactions were just that: the transfer of title to goods for a certain price. From the ultimate independent purchaser, a legal relationship was created between that purchaser and the intermediary Yukos affilliate. There was no 'fake' transaction.*"[46]

90. As for the proposition that it represents unlawful "bad faith" or abuse to structure transactions for the primary purpose of optimising tax benefits, the *Quasar De Valores* Tribunal unremarkably concluded that "*[t]he notion of abusive motivation simply does not fit*" and "*[i]t is difficult to see how it could be otherwise, in a world filled with major corporations openly structuring their businesses through low-tax jurisdictions....*"[47]

91. In addition to the unprecedented legal theory on the basis of which Yukos was arbitrarily attacked, even accepting that theory, the specific taxes assessed to a very significant degree are and were without basis. While there are numerous examples,

---

44 Addendum to Report to Committee on Legal Affairs and Human Rights Rapporteur: Mrs. Sabine Leutheusser-Schnarrenberger, *The circumstances surrounding the arrest and prosecution of leading Yukos executives,* Doc 10368 (24 January 2005), ¶ 11 (Exhibit C53).

45 Report of Committee on Legal Affairs and Human Rights Rapporteur: Mrs. Sabine Leutheusser-Schnarrenberger, *Allegations of politically motivated abuses of the criminal justice system in Council of Europe member states*, Doc. 11993 (7 August 2009), ¶ 125 (Exhibit C107).

46 Exhibit C116, ¶ 68.

47 Exhibit C116, ¶ 74.

this may be demonstrated in the context of (i) value added tax ("*VAT*"), (ii) the double taxation effect on corporation profit tax ("*CPT*") and (iii) fines and penalty interest.

<u>VAT</u>

92. Fully 56% of the re-assessed tax liabilities for 2000-04, or RUR 390 billion (USD 13.59 billion),[48] were in respect of VAT levied on turnover from oil exports of the Yukos trading companies during the relevant periods. This amount alone exceeds the total amount of all outstanding tax liabilities claimed from the Company on the date it was declared bankrupt.[49] The legal theory on which re-assessed VAT was applied to Yukos defies belief; no company other than Yukos has ever been subjected to an even remotely similar theory.

93. VAT is a purely federal tax levied at uniform rates throughout Russia. Thus, whilst different types of operations are taxable at different rates, no VAT economy can be gained by the use of companies in special investment zones. Therefore, the justification given by the Tax Ministry for its assignment of the re-assessed tax liabilities to Yukos did not apply to VAT on any theory.

94. Moreover, throughout the relevant period turnover from oil exports was either exempt from VAT (2000)[50] or levied at a 0% rate (2001-2004),[51] subject only to a requirement that the taxpayer provide specified documentation confirming the fact of export. Accordingly, the re-assessed VAT liabilities assigned to Yukos were in respect of turnover that incurred no tax liability at all.

95. The Tax Ministry held that the exemption/0% rate did not apply to the trading companies' turnover because Yukos had "*not submitted*" the supporting export documentation necessary to claim the rate under Article 165 of the Tax Code. Yukos was therefore held liable for VAT on the trading companies' turnover at the maximum rate, which was 20% in 2000-2003 and 18% in 2004.

---

48 USD 1.08 billion (2000), USD 2.39 billion (2001), USD 2.74 billion (2002), USD 3.90 billion (2003), USD 3.48 billion (2004).

49 Application of the Federal Tax Ministry to the Arbitration Court of Moscow (21 April 2006).

50 Article 5(1)(a) of the Value Added Tax Act 1991.

51 Article 164 of the Tax Code.

96. The Tax Ministry did not dispute that the turnover in question arose from export operations qualifying for the 0% rate. Nor did it dispute that all the necessary documentation had been submitted by the trading companies themselves and accepted by the Tax Ministry at the relevant time. The supporting documentation was moreover available to the Tax Ministry during the audits that gave rise to the re-assessments.

97. Thus, the re-assessed VAT liabilities indisputably arose not from any economic activity incurring tax liability, but from the Tax Ministry's own unprecedented and selective approach to "piercing the corporate veil." The export turnover received and declared by the trading companies was attributed to Yukos, whereas their wholly proper and unchallenged actions claiming the 0% export rate were not.[52] The following passage from the Tax Ministry's decision in 2003 concerning one of the trading companies (Energotrade) is representative of the approach (emphasis added):[53]

> "*...in 2003, Energotrade LLC submitted to the tax authority for its place of domicile separate tax returns for value added tax at the rate of 0 percent, as well as a set of documents to justify using a tax rate of 0 percent and tax deductions.*
>
> *Considering the fact that the revenues of Energotrade LLC (including export revenues) are the revenues of Yukos Oil Company OJSC, in order to justify using a tax rate of 0 percent and tax deductions, documents specified by Article 165 of the RF Tax Code must be submitted to the tax authority for the place of domicile of Yukos Oil Company OJSC. No such Yukos Oil Company OJSC documents were submitted.*
>
> *Therefore, in 2003 Yukos Oil Company OJSC violated Articles 164, 165 of the RF Tax Code by failing to calculate and pay the value added tax on unsupported export transactions...*
>
> *The amount of unpaid value added tax on export transactions was RUR 6,826,447,412.*"

---

52 As a Tax Ministry representative asserted at an 8 August 2005 hearing, the documentation properly submitted by the trading companies "*cannot serve as the declaration of intent of Yukos Oil Company OJSC*" – *See* Record of the Court Proceedings of the Ninth Arbitration Court of Appeal (8 August 2005), ¶ 91 (Exhibit C57). But the entire theory underlying the re-assessments was that Yukos and the trading companies were one and the same for tax purposes.

53 Decision No. 52/985 to Hold the Taxpayer Liable for a Tax Offence (6 December 2004) pp. 91 and 92 (Exhibit C42).

98. The courts upheld this approach as follows (emphasis added):[54]

> *"Based on the provisions of articles 146, 164 and 165 of the Russian Federation Tax Code, the right to apply a 0 percent rate is enjoyed by taxpayers in connection with the sale for export of goods they own after presenting to the tax authority a separate tax return and documents in support of the right to apply this [0%] rate... As in 2001 [sic] the owner of oil and oil products was Yukos Oil Company OJSC, the application of the 0 percent tax rate by the entities involved in the tax evasion scheme... is unlawful.*
>
> *Furthermore Yukos Oil Company OJSC [itself] did not submit to the tax authority tax returns in which it would have stated the amount of revenue shown earlier in the returns of [the trading companies], and documents confirming taxation of this revenue at the 0% tax rate.*
>
> *The [trial] court legally and reasonably pointed out that the tax return submitted by Yukos Oil Company OJSC for value added tax for 2003 cannot be considered, since it does not meet the requirements of tax legislation regarding submission of a VAT tax return for each tax period, which is a month or a quarter, and documents were not submitted at these times confirming the sale of goods for export (arts. 163, 165(10), 174(5) of the Russian Federation Tax Code)."*

99. Thus, the trading companies' submission of the export documentation was disregarded on the circular reasoning that they formed part of a "*tax avoidance scheme.*" Further, the courts refused to allow Yukos itself to rely upon the export documentation that it subsequently submitted in its own name because it had not done so "*in time.*" This was notwithstanding the fact that under Article 165(9) of the Tax Code a taxpayer is permitted to reclaim VAT even if the supporting documentation is submitted outside the time limit:

> *"If the taxpayer later submits documents (or their copies) supporting application of the 0% tax rate, the paid amounts shall be returned to the taxpayer...."*

100. In sum, Yukos was assessed billions of roubles in VAT in connection with sales of crude oil and crude oil products that were unquestionably export sales and, therefore, under Russian law exempt from tax or subject to tax at the 0% rate (*i.e.*, no VAT was owed on these transactions). This approach stood in stark contradiction of the Tax Ministry's own re-attribution theory.

---

[54] Judgment of the Ninth Arbitration Court of Appeal (Case Nos. A40-4338/05-107-9; A40-7780/05-98-90) (16 August 2005) pp. 29, 30 (Exhibit C58).

101. Thus, the conviction for non-payment of VAT by illegal means was particularly perverse, not least because there had been no violation of statutory law. The VAT liabilities only arose because the Tax Ministry on the one hand treated the trading companies' operations as those of Yukos for the purpose of making it liable to pay their taxes, but on the other hand it treated them as separate entities when refusing to take into account the evidence they submitted showing the operations in question qualified for the 0% rate applicable to exports (evidence that was never disputed). And even if the VAT re-assessments could have been foreseen, Yukos' conviction implies that it deliberately created billions of roubles of unnecessary and artificial tax liabilities for itself.

102. As the *RosInvest* Tribunal observed:

> *"The extremely formalistic interpretation of the VAT tax law regarding Yukos and its trading companies to the effect that, though exports were undisputedly not subject to VAT, the documentation also undisputedly submitted by the trading companies could not be used in relation to Yukos and thus Yukos was liable for more than US$ 13.5 billion in VAT related taxes is difficult to accept as a justification for a tax liability the size of which was sufficient to lead Yukos into bankruptcy."*[55]

103. Accordingly:

> *"The Tribunal is not satisfied that the enormous VAT assessment plus fines and interest was a bona fide measure of taxation on Yukos. The staggering scale in addition to the inconsistency of approach between the profit tax assessment and VAT assessment must be seen as evidence of intention towards Yukos which go beyond mere application of the tax law evidence on file and cannot be considered as a bona fide and non-discriminatory treatment."*[56]

104. Endorsing the *RosInvest* finding, the *Quasar de Valores* Tribunal similarly held:

> *"...if the tax authorities were going to attribute to Yukos the transactions carried out in the names of its trading companies, they should also have attributed to Yukos the submission of normal VAT documentation by the trading companies.* ***Given that the export transactions in question were indisputably zero-rated for VAT purposes, the refusal to do so can only seem confiscatory to a degree***

55 Exhibit C109, ¶ 452

56 *Ibid* ¶ 620(a)

> ***which comes close to validating the claims in their entirety on this basis alone.***"[57]

105. It is worth emphasising that had the re-assessed VAT been eliminated from the re-assessments levied against Yukos, Yukos could never have been declared insolvent, its main production company would never have been auctioned out from under it, and Yukos would have remained a going concern fully capable of honoring its obligations to Yukos Capital. Stated differently, disregarding all of the other illegal acts described herein, the Russian Federation's illegal and arbitrary assessment of VAT alone acted to expropriate Yukos Capital's Investment.

Double Taxation of CPT

106. With respect to CPT, in addition to being based upon an unprecedented legal theory and assessed on bases inconsistent with that theory, the tax authorities' re-assessment of CPT created a double taxation effect resulting in new liabilities far exceeding any CPT economy achieved by use of the trading companies.

107. First, although the Tax Ministry's legal theories relied on the fact that Yukos controlled the entire flow of production from extraction to refining and sale, in reality it did not re-assess Yukos' CPT on the basis of the Yukos group's consolidated net income. It only took the high-profit trading companies' net income into account.

108. Second, the net income of the trading companies was not consolidated with that of Yukos, but instead each individual company was taxed separately at the maximum CPT rate and then all resulting liabilities were added together and assigned to Yukos. Since much of Yukos' income came from revenue up-streamed from the trading companies, Yukos was effectively taxed twice on significant amounts of revenue.

109. The resulting double taxation effect can be illustrated by a comparison of the Yukos group's consolidated profits and effective CPT rates within Russia prior to and following the 2000 and 2001 reassessments:[58]

---

57 Exhibit C116, ¶ 82 (emphasis added)

58 Consolidated group figures are taken from the Yukos company group's U.S. GAAP Consolidated Financial Statements of 31 December 2001 (Exhibit C3). Analogous group figures for Russia were not supplied in subsequent annual U.S. GAAP reports, the last of which available on Yukos Oil's website is in respect of 2002.

Figure 1. CPT liabilities of Yukos group, 2000-2001 tax years (expressed in millions of US dollars)						
Year	Net income	CPT paid	Effective rate	Additional reassessed CPT	Effective rate after reassessment	Maximum statutory rate
2000	4704	611	13%	1376	**42%**	**30%**
2001	3585	595	17%	1645	**62%**	**35%**

110. Consequently, the Yukos group's consolidated profits were subjected to an effective CPT rate far exceeding the maximum statutory rate.

Fines and Penalty Interest

111. The total amount of fines assessed to Yukos in respect of the relevant period amounted to RUR 243 billion (USD 8.5 billion).[59] Fines are a form of punishment for the commission of a tax offence.[60] The justification given for the fines was that Yukos had committed the tax offence envisaged by Article 122 of the Tax Code in respect of the re-assessed taxes, namely non-payment or underpayment of tax by illegal means.

112. The applicable fine under Article 122 of the Tax Code is 20% of the unpaid amount, or 40% if the offence is committed deliberately. In the case of repeat offenders, the amount of the fine is increased by 100%, *i.e.* to 80% of the unpaid tax.[61] Yukos was held to have committed the tax offences deliberately and thus fined at the rate of 40% in respect of the re-assessed tax liabilities for 2000, and at the rate of 80% for all subsequent years as a retroactive "repeat offender."

113. In Russian law, tax offences are not strict liability offences. Under Article 109 of the Tax Code, lack of *mens rea* (the subjective or mental element of an offence) on the part of the taxpayer precludes the possibility of conviction. Article 110(1) of the Tax Code provides that a taxpayer has the requisite *mens rea* if it committed the tax offence deliberately or carelessly. Under Article 110(2) of the Tax Code, the question of whether a taxpayer has committed an offence deliberately is determined with reference to a two limb test: (i) was the taxpayer aware of the illegal nature of its

---

59 USD 0.67 billion (2000), USD 1.39 billion (2001), USD 2.51 billion (2002), USD 2.47 billion (2003), USD 1.46 billion (2004).

60 Article 114(1),(2) of the Tax Code.

61 Articles 112(2) and 114(4) of the Tax Code.

actions? and (ii) did the taxpayer desire or consciously allow for the harmful consequences of its actions?

114. Although the Tax Ministry and the courts held that Yukos was guilty of the offence, the *mens rea* was never proven (or even attempted to be proven). In particular, it was not shown that any Yukos officials or representatives were "*aware of the illegal nature of their actions.*" Nor was it possible to demonstrate such guilty knowledge since the re-assessments were based not on any precise or foreseeable tax legislation or case law, but on the unique and unprecedented theories devised by the Tax Ministry specifically for the Yukos case. Indeed, the tax certificates issued in late 2003 (*see* paragraph 69 above) alone preclude any finding of intent. The misapplication of the Russian Tax Code and the improper recourse to certain provisions led to the doubling of the standard fines which was wholly wrong.

115. Further, it was not until the decision of the tax authorities on 14 April 2004 that Yukos executives could be said to have been "aware" of the alleged unlawful nature of their actions (putting the tax authorities' conduct in its most favourable light). However, the April 2004 decision holding Yukos liable in respect of alleged tax offenses committed in 2000 came months after the three-year statute of limitations had expired. With complete disregard for this limitations period and the fact that it is impossible to "repeat" an offence in 2001, 2002 and 2003 when the alleged illegality is not known until 2004, the tax authorities illegitimately and artificially added billions to the purported repeat offences fines.

116. The *RosInvest* Tribunal held:

> *"The US$ 3.8 billion repeat offender fines on the basis of conduct pre-dating the tax audit again appears to the Tribunal as a departure from practice applied earlier and from that granted to other companies and thus to be one part of a cumulative effort to prevent Yukos' ongoing existence."*[62]

117. With respect to penalty interest (as distinct from fines), the total amount assessed to Yukos amounted to RUR 119.7 billion (USD 4.13 billion),[63] or 17.14% of the re-

---

62 Exhibit C109, ¶ 620.

63 USD 1.13 billion (2000), USD 0.97 billion (2001), USD 1.10 billion (2002), USD 0.54 billion (2003), and USD 0.38 billion (2004).

assessed tax liabilities. When the Tax Ministry submitted its claim for outstanding liabilities in the Yukos bankruptcy proceedings, it claimed an additional RUR 10 billion of penalty interest over and above that figure (reflecting penalty interest calculated from the date of the re-assessments to the date of the commencement of the bankruptcy proceedings), bringing the total amount of assessed penalty interest to RUR 130 billion.

118. Further, Article 75 of the Tax Code requires the payment of penalty interest on tax arrears. Penalty interest is calculated daily at the rate of .003% of the Russian Central Bank refinancing rate. Article 75(3) of the Tax Code expressly prohibits the accrual of penalty interest where the taxpayer is unable to pay due to imposition of freezing orders by the Tax Ministry or courts restraining use of the taxpayer's property.

119. As discussed in greater detail below, on 15 April 2004, the day after Yukos was presented with the first re-assessment, the Tax Ministry applied for and obtained court orders freezing all of Yukos' assets with the exception of oil and oil products.[64] The company's property remained frozen (and was subjected to concurrent freezing orders arising from the re-assessed tax liabilities in respect of the 2001-2003 tax years) until the Arbitration Court of Moscow commenced bankruptcy proceedings and appointed an interim receiver for Yukos on 28 March 2006. Nonetheless, and in derogation of Article 75(3) of the Tax Code, penalty interest was calculated retroactively and continued through the day the Company was placed under insolvency supervision.

120. Yukos challenged the assessment of penalty interest in the Russian courts, which challenge was rejected on the unbelievable grounds that Yukos had failed to prove a "*causal link*" between the freezing orders and its inability to pay:[65]

> *"The court does not accept this argument since, despite the taxpayer's documents submitted to the case file about freezing of money, it did not submit evidence that there is a causal link between the impossibility of paying the arrears and the existence of [the] freezing [Order]. In addition, in the court's proceedings, the tax authority presented certificates from Yukos Oil Company OJSC about the voluntary payments of tax arrears under writs of execution during the period of*

---

64 Ruling of the Moscow Court of Arbitration dated 15 April 2004 (Exhibit C18).

65 Judgment of the Moscow Arbitration Court (Case Nos. A40-4338/05-107-9; A40-7780/05-98-90) (28 April 2005) pp. 59 (Exhibit C56).

[the freezing Orders], which indicates the lack of the impossibility for it to pay the arrears due to freezing its property."

121. This conclusion was reached notwithstanding the fact that the court was aware of the scope and nature of the assets frozen to secure the re-assessed tax liabilities. The court's reliance on Yukos' offers to voluntarily pay the tax liabilities was specious, as Yukos made clear that its offers to pay were contingent on the freezing orders being lifted (*see* discussion of enforcement below).

(b) The Enforcement Story

122. As noted previously, the 2000 Tax Assessment was just the first in a series of re-assessments which ultimately subjected Yukos to approximately RUR 692 billion (USD 24 billion) of additional tax liabilities. The tax re-assessments, coupled with the Russian State's enforcement actions, were used first to illegally take Yukos' primary production subsidiary and then to leverage Yukos into an orchestrated bankruptcy where it was, ultimately, dissolved as a company and removed from the companies register in Russia.

123. On the same day as the 2000 Tax Assessment was issued, 14 April 2004, the Russian Tax Ministry issued Orders to Pay requiring that Yukos pay the purported taxes, fines and penalties described therein.[66] The Orders to Pay specified that the total amounts said to be due (approximately RUR 99.4 billion) should be paid by 16 April 2004, the second day after the 2000 Tax Assessment and Orders to Pay had been adopted.

124. On 14 April 2004, even before the ludicrous two-day period to pay the 2000 Tax Assessment had expired (and not having properly served Yukos), the Tax Ministry commenced legal proceedings with the Moscow Court of Arbitration to recover the RUR 99.4 billion in re-assessed taxes, fines and penalties.[67] On the very same afternoon, the Ministry applied *ex parte* for an injunction order securing payment of the amounts at issue.[68] This application for an injunction was also filed before the two-day period for paying the 2000 Tax Assessment had expired. Having given

66 Resolution No. 14-3-05/1609-1 to Hold the Taxpayer Fiscally Liable for a Tax Offence (14 April 2004) (Exhibit C13), Tax Payment Demand No. 14-3-05/1610-8 of 14 April 2004 (Exhibit C14), and Tax Penalty Payment Demand No. 14-3-05/1611-1 of 14 April 2004 (Exhibit C15).

67 Petition of the Tax Ministry for the Recovery of taxes, penalties and fines from OAO NK Yukos dated 14 April 2004 (Exhibit C16).

68 Application by the Ministry of Taxes for Remedial Measures dated 14 April 2004 (Exhibit C17).

Yukos no opportunity to respond to the Assessment and Orders to Pay, the Ministry nonetheless represented to the court that "*the taxpayer does not intend to pay the taxes.*" On this basis, the Ministry sought to freeze all of Yukos Oil's assets.

125. Before the close of business on 15 April 2004, the Moscow Court of Arbitration accepted jurisdiction of the enforcement proceeding, issued the requested injunction and issued writs of execution (again, all on an *ex parte* basis before Yukos was given an opportunity to respond to the 2000 Tax Assessment and before the two-day voluntary payment period had run).[69] On 16 April 2004, writs of execution were issued by the City of Moscow court bailiff.

126. On 22 April 2004, Yukos challenged the injunction on the basis that it was grossly disproportionate, covering assets worth approximately 5.5 times the amount of the total tax liability asserted in the 2000 Tax Assessment. The Moscow Court of Arbitration rejected this challenge the next day.[70]

127. The hearing on the Tax Ministry's enforcement proceeding began on 21 May 2004 and concluded on 26 May 2004, following which the court substantially granted the petition for the recovery of taxes.[71] As with most proceedings relating to Yukos, the hearing was a sham and the result predetermined. Due process was nowhere to be found. Among other things, the Tax Ministry filed approximately 24,000 pages of documents with the court on 17 May 2004, a further approximately 45,000 pages on 18 May and another 2000 late on 20 May, the eve of the hearing. These materials were not evaluated by the court, which simply adopted the submissions of the tax authorities, and Yukos was given virtually no opportunity to review, assess and respond to them.[72]

---

69 Determination of the Court of Arbitration Accepting Jurisdiction (15 April 2004) (Exhibit C19), Determination of the Moscow Court of Arbitration dated 15 April 2004 (Exhibit C20), Writs of Execution dated 15 April 2004 (Exhibit C21).

70 Resolution of the Moscow Arbitrazh Court (23 April 2004) (Exhibit C22).

71 *See* Award of the Moscow Arbitration Court of 26 May 2004 (Exhibit C23).

72 As Yukos observed in its appeal of the court's decision, "*The Russian Tax Ministry's argument that the Defendant's representatives had reviewed the tens of thousands of documents in the course of 2 days of visiting the Ministry, where they were not shown any documents at all (instead being directed to stacks of seemingly random and unclassified photocopied pages piled in vegetable crates...) can hardly be treated seriously.*"

128. Thereafter, through procedural maneuverings the Tax Ministry caused the courts to shorten the time period that should have been available to Yukos to appeal the result of the enforcement proceeding, and the courts rejected Yukos' applications for more time. On 29 June 2004, the Moscow Court of Arbitration rejected the appeals and upheld the first instance decision, only marginally decreasing the amount of Yukos' tax liability for the year 2000, bringing the alleged liability to RUR 99.3 billion (USD 3.42 billion).[73]

129. Enforcement was commenced on 30 June 2004, with writs of execution issued by the Moscow City bailiff before the written judgment of the appeals court was finalized,[74] and despite the Tax Ministry having three years in which to proceed with the actual collection of the 2000 alleged tax debt. Yukos was required to make voluntary payment within five working days, failing which a further and substantial administrative charge (*i.e.*, a 7% surcharge – USD 239.55 million[75]) would be levied on the outstanding balance and forced execution actions would be taken. In addition, the enforcement order was served on Yukos' banks so that balances in its accounts were declared forfeit to the Tax Ministry in immediate partial satisfaction of the 2000 Tax Assessment.

130. On 1 July 2004, a series of seizures of Yukos' non-monetary assets began. These seizures covered virtually all of Yukos' holdings in its subsidiaries, whose value far exceeded the purported 2000 tax liability. The enforcement order by its terms made voluntary compliance impossible by arresting all of Yukos' assets (as did the injunction of 15 April 2004). Further, the possibility of Yukos obtaining interim measures to stay enforcement pending further appeal was non-existent because any such application would need to be accompanied by security and the terms of both the bailiff's enforcement order and the 15 April 2004 injunction precluded this (Yukos appealed nonetheless, which appeals were all rejected by February 2005).

---

73 Judgment of the Moscow City Arbitration Court of 29 June 2004 (9 July 2004) (Exhibit C27). The RUR/USD exchange rate was 29.0274/1 as reported by the Central Banks of Russia on 30 June 2004.

74 Determination on the Initiation of Execution Proceedings dated 30 June 2004 (Exhibit C25).

75 USD 3.42 billion and USD 239.55 million were approximately equivalent to 9,333,836,391 and 6,953,375,547.37 rubles respectively, as at June 30, 2004.

131. On 30 June 2004, the Tax Ministry issued its tax reassessment report for the year 2001, having commenced a tax inspection on 23 March 2004. Yukos was subject to an additional tax liability for the year 2001 amounting to approximately RUR 100 billion (approximately USD 3.4 billion[76]).

132. The intent of the Russian State, of course, was to ensure that Yukos could not pay the trumped-up tax liabilities, thus rendering its assets subject to seizure and sale. Indeed, on 1 July 2004, Yukos pointed out to the bailiff that it could not comply with the requirement to pay the 2000 liability voluntarily because of the arrest of its assets. Yukos nevertheless noted that it was the registered owner of a 34.5% stake in the total share capital of Sibneft as a result of the merger of the two companies in Autumn 2003. Yukos proposed that this holding be sold to meet its total tax liability for 2000 provided that the arrest and injunction were lifted.[77] This proposal was rejected by the bailiff despite the requirements under Russian law that: (i) the debtor determine the type and parts of its property that are to be subject to execution (*see* Article 46(5) of the Russian Federal Law on Enforcement Procedure) and (ii) where monetary assets are insufficient, recourse should be had first to assets which are not central to the debtor's business or livelihood (*id.*). Yukos made the same proposal in an "*Application for Voluntary Compliance*" to the Ministry of Justice, again to no avail. (This was just one of numerous offers made by Yukos to settle or otherwise arrange for payment of the purported tax liabilities, all of which were rejected or ignored.)

133. On 9 July 2004, the Moscow bailiffs imposed the 7% surcharge in their own favour and, on 14 July, seized the shares in Yukos' three principal production subsidiaries, Yuganskneftegaz ("*YNG*"), Samaraneftegaz and Tomsneft. These three companies were responsible for the vast majority of the oil and gas production of the Yukos group, with YNG alone responsible for approximately 60% of crude oil production.

---

76 Report No. 30-3-14/1 on the Repeat Field Tax Audit Report of Yukos Oil Company dated 30 June 2004 (5 July 2004) (Exhibit C26). Based on a RUR/USD exchange rate of 29.0409/1 reported by the Central Bank of Russia on 5 July 2004.

77 *See* Decision of the Moscow City Arbitration Court of 6 August 2004 (13 August 2004) (Exhibit C29). Based upon contemporaneous quoted prices for Sibneft shares, the market value of the interest held by Yukos was in the range of USD 4.05 billion to USD 4.65 billion, well in excess of the liability asserted in the 2000 Tax Assessment. In its opposition to the 15 April 2004 injunction, Yukos unsuccessfully argued that the injunction should extend only to the Sibneft holding for the same reason.

134. Surprisingly, on 2 August 2004, the Moscow Court of Arbitration granted an application by Yukos challenging the bailiff's surcharge and, on 6 August, granted Yukos' challenge to the seizure of the YNG shares.[78] The effect of both decisions was short-lived. On 9 August 2004, the bailiffs announced in a press release that the YNG shares had been "*re-seized*" and, on 18 August 2004, the Ninth Appeal Arbitration Court granted the bailiff's appeal against the 6 August order and ordered the YNG shares seized again (an appeal of this decision was rejected in October).[79] On 25 August 2004, the appeal court re-instated the bailiff's surcharge. Having apparently gotten the message, and in similar fashion, on 12 August 2004, the Moscow Arbitration Court rejected a proposal by Yukos to pay in installments because there were "*no exceptional circumstances*".[80]

135. On 2 September 2004, the Tax Ministry adopted a tax assessment decision for 2001 based upon the 30 June report (the "*2001 Tax Assessment*").[81] The 2001 Tax Assessment asserted that Yukos was liable for tax for that year of RUR 50.8 billion together with penalty interest of RUR 28.5 billion. It also included fines calculated at the basic figure of RUR 20.3 billion and then doubled to RUR 40.6 billion to take account of Yukos' purported recidivism. The total liability asserted under the 2001 Tax Assessment was therefore RUR 119.9 billion (USD 4.1 billion).[82]

136. Also on 2 September 2004, the bailiffs commenced direct enforcement proceedings in respect of the tax and penalty interest elements of the 2001 Tax Assessment (*i.e.*, the Tax Ministry did not bother to first obtain a court order validating the tax assessment). This was blatantly unlawful, as Russian law precludes direct enforcement where the tax assessment involves a re-classification of the nature of the tax payer's transactions. The bailiffs then consolidated the enforcement proceedings in relation to each of the 2000 and 2001 Tax Assessments, thus accelerating the legal process with respect to 2001.

---

78 Decision of the Moscow City Arbitration Court of 6 August 2004 (13 August 2004) (Exhibit C29).

79 Ruling of the Ninth Arbitration Court of Appeal of 18 August 2004 (23 August 2004) (Exhibit C31).

80 Ruling of the Moscow Arbitration Court dated 12 August 2004 (Exhibit C28).

81 Decision No. 30-3-15/3 Holding a Taxpayer Liable for a Tax Offences dated 2 September 2004 (Exhibit C32).

82 Based on the RUR/USD exchange rate of 29.2552/1 reported on 2 September 2004 by the Central Bank of Russia.

137. Similar to the 2000 Tax Assessment, on 2 September 2004 the bailiffs adopted an Order to Pay for 2001 which gave Yukos until 4 September to pay the 2001 Tax Assessment in full.[83] Even more ludicrous, the 2001 Order to Pay was served on Yukos on 3 September, 4 September being a Saturday. While academic given then existing circumstances, Yukos effectively was given less than one day to arrange payment of the entire 2001 Tax Assessment. With Yukos unable to pay due to the various State-imposed restraints on its assets, the bailiffs adopted enforcement decisions for 2001, froze the company's assets yet again (thirteen times in September 2004 alone) and provided for a five-day period for payment after which a 7% surcharge would be levied. Needless to say, this was followed by the imposition of the surcharge for 2001.

138. This pattern of "direct enforcement" repeated itself with respect to 2002 and 2003. On 16 November 2004, the Tax Ministry adopted an assessment for 2002 in the amount of RUR 193.8 billion (USD 6.76 billion[84])-the largest of the five alleged reassessments-and, on 6 December 2004, an assessment for 2003 was adopted for a further RUR 170.3 billion (USD 6.1 billion[85]). The 7% surcharges were duly added for failure to pay within the time periods set by the court bailiffs. The Tax Ministry even went a step further with respect to 2002 and 2003, refusing to consider the written objections submitted by Yukos on the frivolous ground that they were not presented personally at the Tax Ministry but served by post. The purpose of this unseemly haste was to ensure that Yukos Oil's outstanding tax liabilities remained large enough to support the Ministry's case for the forced auction of YNG, Yukos' core production subsidiary (*see* below).

139. To briefly summarise, by August-September 2004, the Russian State had assessed Yukos approximately RUR 220 billion (USD 7.5 billion) in trumped-up tax liabilities for 2000-01 and ensured that Yukos would be unable to pay those liabilities through (i) multiple orders freezing its assets and (ii) refusing its proposal to sell liquid assets

---

83 Tax Payment Demand No. 133 dated 2 September 2004 (Exhibit C33).

84 Decision No. 52/896 to Hold the Taxpayer Liable for a Tax Offence dated 16 November 2004 (Exhibit C37). The RUR/USD exchange rate was 28.6696/1 as reported on 16 November 2004 by the Central Bank of Russia.

85 Decision No. 52/985 to Hold the Taxpayer Liable for a Tax Offence dated 6 December 2004 (Exhibit C42). On 6 December 2004, the RUR/USD exchange rate was 27.9271/1 as reported by the Central Bank of Russia.

such as the Sibneft shares and other settlement offers. By early December 2004, the 2002-03 tax years had been thrown into the mix, increasing the total liability to approximately RUR 585 billion (USD 20.3 billion). All of this was done in gross violation of Russian and international law.

(c) The Forced Auction of Yuganskneftegaz

140. With the stage thus set, the Russian State proceeded with the next phase of its plan: the gutting of Yukos by the illegal taking of YNG, its principal production subsidiary, and engineering its "sale" to a State-owned company.

141. On 12 August 2004, the Russian State commissioned Dresdner Kleinwort Wasserstein ("*DKW*") to perform a valuation of the participation to be sold in YNG.[86] DKW's report, dated 6 October 2004, valued the share capital of YNG at USD 15.7-18.3 billion.[87] At the same time, the Russian Federation sought to depress the value of YNG by calling into question the validity of the company's licenses.[88]

142. Yukos Oil commissioned a separate valuation by JPMorgan. In JPMorgan's report dated 27 October 2004, YNG's shares were valued at USD 16.1-22.1 billion.[89] (Reports from other neutral observers valued YNG in excess of USD 30 billion.)

143. In early November 2004, Yukos announced that it would hold a shareholders meeting on 20 December 2004 to consider whether the company should file for bankruptcy. Among other things, a bankruptcy filing would have acted to stay legal proceedings against Yukos, including enforcement against its assets.

144. On 18 November 2004, the Chief Directorate of the Ministry of Justice of the Russian Federation for Moscow and the Russian Federal Property Fund (the "RFPF"), a specialised State institution, concluded a contract according to which the RFPF undertook to sell Yukos' shares in YNG "*in an amount no less than 246,753,447,000.18 roubles.*" This price bore no relation to any of the available valuations, but rather corresponded to the total outstanding tax liability at that time.

---

86 The Russian Federation had publicly announced its plan to sell Yuganskneftegaz on 20 July 2004.

87 ZAO Dresdner Bank Valuation Report of Yuganskneftegaz dated 6 October 2004 (Exhibit C34).

88 *Yuganskneftegaz may lose licenses in three months*, RIA Novosti, 11 October 2004 (Exhibit C35).

89 JPMorgan Valuation Report of OAO Yuganskneftegaz dated 27 October 2004 (Exhibit C36).

On the same day, by order of the acting Chairman of the RFPF, an auction commission was appointed.

145. In an issue of *Rossiyskaya Gazeta* dated 19 November 2004, an information notice was published concerning the auction to sell the frozen shares in Yuganskneftegaz.[90] The notice indicated the number of shares to be sold, *i.e.*, 43 ordinary shares, and the starting sale price, *i.e.*, 246,753,447,303.18 roubles. The date for the auction was set for 19 December 2004, the day before the scheduled meeting of Yukos shareholders (and, incidentally, a Sunday).

146. Yukos challenged the planned auction in the Russian courts, which challenges were rejected,[91] and Yukos was enjoined from holding an emergency meeting of its shareholders in advance of the auction.

147. With few remaining options, Yukos sought the protection of the United States Bankruptcy Court for the Southern District of Texas.[92] By judgment dated December 16, 2004,[93] Yukos obtained an order from the Bankruptcy Court temporarily restraining certain entities from taking any action in the auction.[94] The Bankruptcy Court noted that the evidence before it suggested that "*the Debtor [i.e., Yukos] has assets other than [Yuganskneftegaz] from which to begin to satisfy the amount assessed by the tax authorities, as commonly permitted under Russian law... [and] that the authorities refused to consider other assets, and insisted on the sale of Yuganskneftegaz.*"[95] In granting the injunction, the court found that:

> *"Participants in international commerce, in Russia, in the United States, and elsewhere, need to have an expectation that when they invest in foreign enterprises they may do so without fear that their investments may be subject of confiscatory action by agencies of the foreign government. In the instant case, the appearance to the plaintiff,*

---

90 Notice of auction published by the Russian Federal Property Fund in Rossiyskaya Gazeta on 19 November 2004 (Exhibit C38).

91 Ruling of the Moscow Arbitration Court dated 29 November 2004 (Exhibit C40); Decision of the Moscow Arbitration Court dated 3 December 2004 (Exhibit C41).

92 Voluntary Petition by Yukos Oil Company filed on 14 December 2004 (Exhibit C43).

93 *Yukos Oil Co. v. Russian Federation*, United States Bankruptcy Court for the Southern District of Texas, Houston Division, Case No. 04-47742-H3-11, Adv. no. 04-3952 (16 December 2004) (Exhibit C44).

94 Namely, OOO Gazpromneft, ZAO Intercom, OAO First Venture Company, ABN Amro, BNP Paribas, Calyon, Deutsche Bank, JPMorgan and Dresdner Kleinwort Wasserstein.

95 Exhibit C44 ¶ 19.

> *and its investors, of such a confiscation, is created by what appears, on the evidence before this court, to be the inconsistent application of Russian law within the Russian legal system."*[96]

148. Notwithstanding the US court injunction, the Russian Government proceeded with the YNG auction on 19 December 2004. According to the official protocol there were two participants, OOO Baykalfinansgrup (or Baikal Finance Group) and OOO Gazpromneft. (As reported in the Addendum to the European Parliamentary Assembly Report, "*other potential bidders, including from abroad, were discreetly 'discouraged' from participating.*")[97] Gazpromneft was, until the day before the auction (when it was sold to an unknown third party), a wholly owned subsidiary of OAO Gazprom, the largest gas company in the world and largely controlled by the Russian State. At the time of the auction, the CEO of Gazpromneft was Sergey Bogdanchikov, the President of Rosneft. As was later revealed (*see* below), Baikal Finance Group was a shell company created to insulate Rosneft from potential liability and function as a conduit for the eventual transfer of YNG into State hands.

149. While there were officially two participants in the auction, only one of the participants actually bid, Baikal Finance Group. Gazpromneft did not. Baikal Finance Group won the auction with its opening bid of USD 9.35 billion (half of YNG's conservatively estimated value), the whole bidding process lasting approximately ten minutes. As it turns out, Baikal Finance Group was a Rosneft affiliate[98] established on 6 December 2004 at Tver in central Russia, at an address housing a fast food restaurant, a mobile phone shop and a liquor store. In other words, Baikal Finance Group was formed solely for purposes of the auction and the auction itself was then staged to arrive at a pre-determined, low-ball result, all in clear violation of Russian and international law.

150. Any mystery about who was behind the auction scam was removed in the week following the auction. On 21 December 2004, in the Gottorf Castle of Schleswig-Golstein Land in Germany, a press conference with then Russian President V.V. Putin

---

96 *Ibid* ¶ 138.

97 Addendum to Report to Committee on Legal Affairs and Human Rights Rapporteur dated 24 January 2005 (Exhibit C53), ¶ 12.

98 List of Affiliated Persons: Public Joint Stock Company "Rosneft Oil Company" (30 September 2007) (Exhibit C94).

and German Chancellor G. Schroeder was held at which the following exchange occurred:

> *"QUESTION: Dear Mr President, another question about Yukos. What do you think about the opinion that a State company is in fact behind the organisation Baikal Finance Group?*
>
> *MR PUTIN: As is well known, the shareholders of this company are all private individuals, but they are individuals who have been involved in business in the energy sphere for many years. They intend, as far as I am informed, to establish relations with other energy companies in Russia which have an interest in their company. And within the framework of current legislation, the participants of this process have the right to work with this company after the auction is held. For us, it is only important that all these actions, as I already said, are within strict accordance with the current legislation of Russia. I hope that this is the way it will be. As for the ability of state company to buy these assets, they of course have this right, just like other market participants."*[99]

151. Two days later, on 23 December 2004, a Rosneft Oil Company official announced Rosneft's "purchase" of Baikal Finance Group.[100] The company was purchased for a token price of USD 360 (an amount corresponding to Baikal Finance Group's share capital). It was later revealed that Rosneft had coordinated and provided the financing for the YNG purchase. At the time, Rosneft was entirely owned by the Russian State and no less than 10 of its 11 directors combined their directorial duties with State office, either in the Russian Government or the Presidential Administration.

152. The same day, at a press conference dedicated to events of 2004, President Putin declared the following in response to a question about the Rosneft's acquisition of the shares in YNG:

> *"Essentially, Rosneft, a 100% state owned company, has bought the well-known asset Yuganskneftegaz ... Now what would I like to say in this context? You all know only too well how the privatisation drive was carried out in this country in the early 90s and, how, using all sorts of stratagems, some of them in breach even of the then current legislation, many market players received state property worth many billions. Today, the state, resorting to absolutely legal market*

---

99 Press Statements and Answers to Questions Following Russian-German Bilateral Consultations, Gottorf Castle, Schleswig-Holstein, Germany (21 December 2004) (Exhibit C45).

100 The Guardian, *State steps in for Yukos unit* (23 December 2004) (Exhibit C46).

> *mechanisms, is looking after its own interests. I consider this to be quite logical."*[101]

153. President Putin made similar comments to a group of Spanish journalists in February 2006:[102]

> *"Q: Mr. President, as they say in the film: everything you wanted to know but were afraid to ask ... Why does the [Russian] State use non-transparent schemes? For what purpose? It used Baykalfinansgrup to buy Yuganskneftegaz. It used the same scheme with Rusukrenergo to deliver gas to Ukraine. Why do you need these schemes?*
>
> *PUTIN: I'll tell you why ...*
>
> *Q: Sometimes it seems that it is to avoid taxes. Even the Northern [sic] Gas Pipeline has its legal address in Switzerland, if I'm not mistaken.*
>
> *Regarding Baikalfinancegroup, the situation is quite simple. This was not an administrative or repressive issue, but a legal issue. The future owners had to think about how they were going to work and how they would perhaps have to respond to lawsuits in the court, if such ever arose. When Baikalfinancegroup acquired the corresponding stake it became the owner and everything that took place subsequently took place on the secondary market. This meant that claims against those who had acquired these assets were reduced to practically nil.*

154. President Putin's disingenuous comments were expressed in rather plainer language by the Russian Presidential Advisor for Economic Matters, A.N. Illarionov, who remarked, at a 28 December 2004 press conference, that (emphasis added):

> ***"This year, without any doubt, the leader for the nomination of Scam of the Year is the sale of Yuganskneftegaz to the mystical company, although now not so mystical, Baikalfinansgroup by Rosneft,*** *all the operations merging Rosneft and Gazprom, separating Rosneft and Gazprom, and so on. Before now we saw such actions by confidence tricksters, but now we see that companies with 100% State capital and government authority do this....This story clearly showed that the game has no rules and that the rules change constantly for the benefit of rather specific interests of the moment."*
>
> *In this sense, the whole scam unfortunately demonstrates that all of the official or semi---official reasons offered to the public about the Yukos*

---

[101] Press Conference with Russian and Foreign Media, The Kremlin, Moscow (23 December 2004) (Exhibit C47).

[102] Interview to the Spanish Media, The Kremlin, Moscow (7 February 2006) (Exhibit C63).

> *case are completely unfounded. It's not about whether Yukos had violations or whether or not it had back taxes, because in this case no one cared about back taxes. The company began to pay back taxes even when it didn't recognize the validity of the claims, and it was even ready to pay astronomical amounts, but no one was interested.* ***Additional tax payments were refused in order to take the asset. And this is the most dramatic and most earnest declaration of the actual intent behind the whole Yukos case.***"[103]

It comes as no surprise that Mr Illarionov was later punished for his candour.

155. As summed up in the Resolution of the European Parliament, the auction of YNG yielded "*a price far below the fair market-value*" and was the result of Yukos being "*forced to sell off its principal asset, by way of trumped-up tax reassessments leading to a total tax burden far exceeding that of Yukos's competitors, and for 2002 even exceeding Yukos' total revenue for that year.*"[104] The result, as stated concisely in the Addendum to the Parliamentary Assembly Report: "*Yuganskneftegaz has effectively been re-nationalised.*"[105]

156. The *RosInvestCo* Tribunal had no difficulty reaching the same conclusion:

> *"[T]he Tribunal concludes that the auction on 19 December 2004 in which Baikalfinansgroup company, a front for Rosneft, acquired Yukos' main asset, the YNG shares, was organised in a manner to ensure state control was ultimately asserted over the asset. In short the Tribunal is convinced that the auction of YNG was rigged."*[106]

(d) The Forced/Sham Bankruptcy of Yukos Oil

157. With Yukos Oil's principal production subsidiary taken and its remaining assets frozen as security for the outstanding tax "liabilities," the stage was set for the Russian State end game. In June 2004, then President Putin assured the world that "*Russian authorities, the government, and the economic officials of our country are not interested in seeing Yukos go bankrupt ... The government will try to do everything*

---

103 Translated extract from the Speech by Andrei Illarionov, Presidential Advisor on Economic Affairs, on 28 December 2004: http://www.iea.ru/econom_rost.php?id=7 (Exhibit C48); The Moscow Times, 11 January 2005 (Exhibit C52); BBC News, 28 December 2004 (Exhibit C49); The New York Times, 4 January 2005 (Exhibit C50); The Economist, 6 January 2005 (Exhibit C51).

104 European Parliament Resolution 1418, *The circumstances surrounding the arrest and prosecution of leading Yukos executives* (25 January 2005), ¶ 13 (Exhibit C54).

105 Exhibit C53, ¶ 12.

106 Exhibit C109, ¶ 620.

not to topple this company."[107] By late 2005, the State commenced the final phase of its plan to do just that.

158. One of Yukos Oil's largest creditors was a group of Western lenders under a USD 1 billion syndicated loan agreement dated 24 September 2003. By secret agreement with this group of banks dated 13 December 2005, Rosneft orchestrated the commencement of bankruptcy proceedings for Yukos.[108] Essentially, the agreement worked as follows: Rosneft agreed to purchase the debt held by the lenders, thus satisfying the lenders' claims and stepping into their shoes, provided the lenders agreed to first (i) "*endeavour to file and have accepted the Application for Bankruptcy ... as soon as is reasonably practicable*" and (ii) take whatever steps were then required to substitute Rosneft for the lenders in the bankruptcy case. In this way, the Russian Federation sought to have Yukos thrown into bankruptcy proceedings without having it appear that such proceedings were being commenced by it or at its behest (albeit rather clumsily).

159. Pursuant to the above agreement, the banks made a formal application for a bankruptcy order on 6 March 2006,[109] Rosneft was substituted for the banks as applicant on 14 March 2006[110] and insolvency proceedings were opened on 28 March 2006.[111] In its initial stage, the proceedings were "*supervisory,*" with E.K. Rebgun appointed as temporary receiver and the Yukos board retaining certain authority.

160. Following an initial period during which the recognition of Yukos "creditors" was manipulated by the State, a creditors meeting was held on 20 July 2006 and later adjourned until 25 July 2006. The purpose of the meeting was to determine whether, among other things, a financial rehabilitation plan should be instituted for Yukos or, on the other hand, a court petition should be filed requesting that Yukos be declared bankrupt and formal liquidation proceedings commenced. Twenty-four creditors

---

107 "Putin Says Russia Wants Yukos to Survive," Seth Mydans, The New York Times (18 June 2004) (Exhibit C24).

108 Sale Agreement Relating To Certain Rights And Benefits Arising Under A Credit Agreement dated 24 September 2003 between, amongst others, Yukos Oil Company and Société Générale SA dated 13 December 2005 (Exhibit C62).

109 Banks' Petition to declare Yukos bankrupt filed with the Moscow City Arbitration Court on 6 March 2006 (Exhibit C64).

110 Yukos was notified and the Moscow Arbirazh Court formalised the transition on 28 March 2006.

111 Ruling of the Moscow Arbitrazh Court of 28 March 2006 (29 March 2006) (Exhibit C65).

were permitted to participate and vote, with votes allocated based upon the size of each creditor's claim. Representatives for Yukos made a presentation demonstrating that its market value was estimated to be approximately USD 38 billion, almost USD 20 billion in excess of its purported liabilities (including the tax re-assessments). Applying wholly inappropriate "fire sale" discounts ranging as high as 40%, and discounting further for a 24% profit tax said to be payable on any liquidation sales, Mr Rebgun arrived at a valuation of approximately USD 17.75 billion[112] (which-very conveniently-was not sufficient to cover the USD 18.3 billion of registered claims) and took the position that "*The current activities of OAO 'YUKOS Oil Company' may be carried out without losses, but the aggregate proceeds from the sale of property and proceeds from the current activities would not cover its obligations to the creditors.*"

161. Votes were then taken. Sixteen creditors present voted for the proposal to institute a rehabilitation plan for Yukos and against filing a petition declaring the company bankrupt. Four creditors took the opposite position, with the remainder abstaining. The result: the proposal to file a petition declaring Yukos bankrupt was approved and rehabilitation rejected. The basis on which this could happen: the four creditors wishing to bankrupt and dissolve Yukos controlled 93.87% of the votes. The identity of those creditors: The Russian tax authorities, Rosneft (the state-owned oil company), YNG (now owned by Rosneft), which had manufactured some trumped-up claims of its own, and one small creditor. Virtually all legitimate creditors sided with Yukos or abstained.

162. By court order dated 1 August 2006, Yukos was formally declared bankrupt and liquidation proceedings commenced.[113] Rebgun was appointed liquidator. Yukos appealed from this judgment but, employing his new powers as liquidator, Rebgun withdrew the required powers of attorney from Yukos' lawyers so no representative of Yukos could appear at the hearing of the appeal and it was, not surprisingly, rejected.

163. The rest of the plan played out more or less according to script, with one exception the Russian State creatively addressed. During the period March-August 2007,

---

[112] *See* Data from the Yukos Interim Receiver's Report dated 24 July 2006 (Exhibit C72).

[113] Decision of the Moscow Arbitrazh Court of 1 August 2006 (4 August 2006) (Exhibit C74).

auctions of Yukos Oil's remaining assets were organised and conducted under Rebgun's supervision. The auctions were, in most respects, similar to the YNG auction-staged events with straw man bidders conducted in violation of domestic and international law where the auctioned assets found their way into the hands of the Russian State (largely Rosneft). Of the seventeen auctions conducted, Rosneft won eight and, in connection with three more, purchased the assets shortly after they were auctioned. The assets obtained by Rosneft generated over 80% of the total auction proceeds.

164. Despite the "fire-sale" prices resulting from the corrupt auctions, a problem arose for the Respondent: the assets marshaled by Rebgun totaled, by end of July 2007, USD 31.07 billion, almost double the USD 18 billion valuation used by Rebgun to justify bankruptcy proceedings and far in excess of even the trumped-up claims of the Russian tax authorities. Put another way, despite Respondent's best efforts, Yukos remained solvent, hence the problem requiring creative solutions. In this, the Russian State was not dissuaded by the requirement under Russian law that bankruptcy proceedings be discontinued whenever there is a demonstrated surplus of assets over the claims of registered creditors (as there was on numerous occasions during the course of the Yukos bankruptcy proceeding). The creative solution was to invent ever more claims, even after the legal period for registration of claims had closed.

165. On 7 August 2007, following an application by Rebgun to extend the receivership period and despite the existing surplus value of Yukos' assets, a three-month extension was granted by the court.[114] During that period of time, Rosneft and the Federal Taxation Service came up with billions in additional "claims."

166. One such claim, the "mismanagement" claim (around USD 5.5 billion), was based on an allegation that Yukos Oil owed damages to YNG for having applied low transfer prices in connection with inter-company purchases of crude oil. This is a wholly spurious claim rendered even more so by the facts that: (i) any such "damage" should have been offset in the rigged price Rosneft paid for YNG (*i.e.*, effectively satisfied by the gross underpayment made to Yukos), and (ii) the "income" YNG claimed to have been deprived of was income improperly attributed to Yukos by the tax

[114] Ruling of the Moscow Arbitrazh Court of 7 August 2007 (8 August 2007) (Exhibit C91).

authorities and which formed part of the basis for the alleged tax assessments (*i.e.*, if that income was to be transferred to YNG as "damages" there is no way Yukos could be held liable to pay tax on it).

167. In addition to the claims for which the tax authorities had obtained court orders (discussed above), they filed additional claims in the bankruptcy for which, as it happens, they had not. In its subsequent claims, the Tax Ministry alleged that taxes generated during the bankruptcy proceedings amounted to approximately USD 9 billion. To substantiate these new claims, the Tax Ministry submitted 127,333 documents which were attached to the court file at the very same time the judgment admitting the claim was pronounced. This was done without the court having so much as looked at the documents and without the representatives of Yukos having been permitted to review them-and also without checking whether (under Russian law) the documents could even serve as evidence.

168. Further, the tax authorities were unable to reconcile the figures they represented to be (i) payments received from Yukos Oil out of the foreclosure sale of YNG and (ii) those same figures reported by the bailiffs following the auction a year before. That is, the tax authorities claimed to have received well over USD 1.5 billion less than the sum the bailiffs reported as having been recovered and thus sought to recover that amount again from the bankruptcy estate. No explanation was given for this discrepancy and repeated requests for an explanation and reconciliation were ignored. Nevertheless, the court allowed the claim in its entirety and its judgment was no more than a verbatim repetition of the unsubstantiated claims of the tax authorities, with the judicial decision even including the same typos.

169. Ultimately, all claims included in the Register of Creditors' Claims were paid in full, with 99.71% of them belonging to the Federal Taxation Service and Rosneft. As discussed below, unlike the former Yukos subsidiaries acquired by Rosneft, those which remained independent of the State had their claims rejected. This included Yukos Capital's claims which are the subject of this Proceeding.

170. Rosneft received approximately USD 10 billion from the bankruptcy according to its financial statements.[115] This amounts to a refund of almost half the entire bargain-basement price it paid for Yukos assets in the purported auctions. The result:

> *"By taking over YUKOS, [Rosneft] the state-run company bypassed its Russian producing and refining competitors, jumping from eighth to first in Russia, where the former YUKOS assets account for over 70% ... The acquisition of Yuganskneftegaz, Tomskneft and Samarneftegaz enables Rosneft to almost quadruple its reserves ..."*[116]

171. In financial terms, the benefit to Rosneft resulting from Respondent's theft of Yukos assets is staggering. Solely by way of example, in July 2006 Rosneft raised USD 10.6 billion in an initial public offering priced at USD 7.55/share. This suggests a 2006 valuation for Rosneft of approximately USD 80 billion. Similarly, for the first six months of 2008 alone (the period immediately following Yukos' bankruptcy), Rosneft reported revenues of USD 37.5 billion and after-tax net income of USD 6.9 billion.[117] More recently, in 2010 and 2011, Rosneft reported revenues of USD 63 billion and USD 91.9 billion, and after-tax net income of USD 10.6 billion and USD 12.5 billion, respectively.[118]

172. It is perhaps interesting to note that, prior to its auction and while still a Yukos affiliate, YNG had itself been hit with re-assessed tax liabilities. The treatment of those claims by the Russian authorities stands in stark contrast with that accorded to Yukos:

> *"Yugansk came with a tax liability of its own, totalling Dollars 4.7bn. In its last annual accounts, Rosneft discloses that a Moscow court decided last month to reduce that claim by over 80 per cent. Those looking for an explanation as to this turn of events might look to the notes in Rosneft's accounts: 'Legislation and regulations regarding taxation in Russia continue to evolve.' Quite."*[119]

---

[115] Rosneft Oil Company OJSC, Interim Condensed Consolidated Financial Statements, Three and six months ended June 30, 2007 and 2006 (Exhibit C89).

[116] Irina Reznik, 'Prosecutor's Discount', Financial Times (25 September 2007) (Exhibit C93).

[117] OJSC Oil Company Rosneft, Interim Condensed Consolidated Financial Statements, Three and six months ended June 30, 2008 and 2007 (Exhibit C102).

[118] Rosneft Oil Company Consolidated Financial Statements as of December 31, 2011 and 2010 and for the years ended December 31, 2011, 2010 and 2009 (Exhibit C114).

[119] Financial Times (26 May 2006) (Exhibit C68).

Rosneft's President also announced that the Russian tax authorities agreed to defer YNG's payment of these vastly reduced liabilities, correctly stating that the authorities were required to accept proposals for deferred payments in accordance with settled court practice in Russia (unless, of course, the debtor is Yukos).[120]

173. By late October 2007, the claims of all registered creditors had been paid, and yet, what little remained of Yukos was not quite dead. Not to be deterred, Rebgun filed an application to terminate the bankruptcy and dissolve Yukos for an alleged deficit said to arise from taxes due on profits from the "auction" sale of Yukos assets. Such a claim was both laughable and a subordinated claim not eligible for inclusion as a matter of Russian law. Nonetheless, Rebgun's application was granted by the court on 12 November 2007,[121] the bankruptcy concluded and Yukos dissolved. Nothing, of course, was left of Yukos for distribution to shareholders.

174. Yukos Capital appealed against the judgment terminating the bankruptcy and at the same time-and in timely fashion-asked for a suspension of the decision to dissolve Yukos.[122] Rebgun took no notice of that request and, on 21 November 2007, Yukos Oil Company was deregistered from the Russian register of enterprises. As a result, it ceased to exist under Russian law and, in a fitting conclusion, Yukos Capital's appeal was rejected by the courts on the circular reasoning that Yukos Oil Company had ceased to exist.[123]

(e) <u>Conclusion</u>

175. The dismantling and destruction of Yukos Oil Company was politically motivated and implemented at the behest of the Russian State through its tax authorities, courts, bankruptcy receiver, State-owned oil company and numerous others. It occurred in abject violation of international law, including Russia's obligations under Part III of

---

[120] OJSC Oil Company Rosneft Consolidated Financial Statements as of December 31, 2007 (Exhibit C99). The full amount of YNG's "liabilities" were, however, taken into account by the State when setting the auction "price" for YNG.

[121] Ruling of the Moscow City Arbitration Court of 12 November 2007 (15 November 2007) (Exhibit C96).

[122] On 26 November 2007, the Ninth Court of Arbitration Appeals dismissed Yukos Capital's declaration for injunctive relief preventing Rebgun from recording Yukos' liquidation in the United State Registry for Legal Entities (Case No. 09AP-16994/2007-GK) (Exhibit C97).

[123] Ruling of the Federal Court of Arbitration of the District of Moscow dated 26 February 2008 (Exhibit C100).

the Energy Charter Treaty. For purposes of this case, the destruction of Yukos expropriated Yukos Capital's Investments.

B. Illegal Acts Directed at Yukos Capital

176. Should the Tribunal be convinced on the merits of the above-described claim (*i.e.*, the dismantling and destruction of Yukos), it need not reach Yukos Capital's claim regarding the Russian State's acts directed specifically at it (which is presented in the alternative). The relevant facts pertaining to Yukos Capital's alternative claim are set forth below.

177. With supervision proceedings having been commenced in March 2006 (*see* above), by application dated 27 April 2006, Yukos Capital sought to have its claims under the Loans included in the register of creditor's claims.[124] At that time, Yukos Capital's claims totaled approximately RUR 118 billion (USD 4.3 billion[125]), inclusive of accrued interest and late repayment penalties. In addition to setting out the details and history of the Loans, Yukos Capital explained that the loan agreements gave it a right to call for early repayment if it had sufficient reason to believe that the financial position of Yukos Oil would prevent it from repaying on time. The application attached supporting documents, including evidence of the transfer of funds to Yukos Oil and Yukos Capital's November 2005 default letter requesting early repayment.

178. Yukos Oil did not object to the application. Rebgun, the Federal Tax Service and Rosneft did, although no objections were made concerning the substance of the loan transactions. Rebgun raised a number of meritless evidentiary points concerning the authority of the individuals who entered into the transactions on behalf of Yukos Oil and Yukos Capital, the receipt of funds by Yukos Oil and the translation of the November letter calling for early repayment of the loans.[126]

179. Rosneft's position was that the loans were not yet due and therefore Yukos Capital did not qualify for inclusion on the register of creditors. Rosneft asserted, contrary to the express terms of the Loan agreements, that debt due under the agreements could not

124 Application for Inclusion of a Claim by Yukos Capital S.a.r.l. in the Registry of Claims of Creditors of Yukos Oil Company OJSC dated 27 April 2006 (Case No. A40-11836/06-88-35 B) (Exhibit C66).

125 On 27 April 2006, the RUR/USD exchange rate was 27.3921/1 as reported by the Central Bank of Russia.

126 Objections to the Claims of Yukos Capital S.a.r.l. filed by the Temporary Receiver for Yukos Oil Company OJSC dated 31 May 2006 (Exhibit C69).

be unilaterally accelerated and could become payable early only pursuant to a court decision. Rosneft supported its arguments by reference to provisions of the Russian Civil Code, disregarding the fact that the Loan agreements were expressly subject to New York law.[127]

180. The Federal Tax Service also argued that the Loans were not yet due. It stated that the Loans had been made in order to fund payment of the claims made by the tax authorities. In particular, it claimed that the December 2003 Loan had in fact been made in January 2006, a claim that was entirely unsubstantiated and contrary to incontrovertible evidence before the court. As further evidence of the fact that the Loans were not due for repayment, the Federal Tax Service cited a Yukos Oil note to the tax authorities dated 15 May 2006, in which the Loans were included in the section headed "Long Term Liabilities."[128] The Federal Tax Service also introduced another allegation: that "*in reality, Yukos Oil Company OJSC had reserved its funds for the purpose of settling the claims of the tax authorities.*" There was no explanation of the relevance of this allegation or justification for it and the Federal Tax Service did not suggest that, as a result, the transactions between Yukos Capital and Yukos Oil were invalid.

181. On 19 July 2006, the Moscow City Arbitration Court issued a ruling denying the inclusion of Yukos Capital's claims in the register of creditors' claims on the basis that the Loans were not yet due.[129] The court's written decision was virtually identical to the submissions of the Federal Tax Service. The court made no attempt to consider or evaluate Yukos Capital's claim and the evidence supporting it. It did not address the actual terms of the Loans or question the assertions made by the objecting parties, despite the fact that they were clearly in conflict with the evidence.

182. On or about 28 July 2006, Yukos Capital filed an appeal from the denial of entry of the Loans into the Registry of Claims.[130] This process was interrupted when, by order dated 8 August 2006, the Russian Prosecutor General's office initiated a

---

127 Objections of Rosneft Oil Company OJSC regarding the claims of Yukos Capital S.a.r.l. for Inclusion of its Claim in the Registry of Yukos Oil Company OJSC Creditors dated 23 May 2006 (Exhibit C67).

128 *See* Minutes of the Court Proceeding of the Moscow City Arbitration dated 12 July 2006 (Exhibit C70) and Ruling of the Moscow City Arbitration Court dated 17 July 2006 (19 July 2006) (Exhibit C71).

129 *Ibid.*

130 Appeal to the Moscow Court Decision from 19 July 2006 (28 July 2006) (Exhibit C73).

criminal case against Yukos Capital and certain individuals.[131] The criminal proceeding was said to have been commenced on the basis of a report forwarded to the Prosecutor General's office by the deputy director of the Federal Tax Service. Yukos Capital has never seen this report, but from the court's order it appears to have been derived from many of the same issues underlying the tax authorities' "re-assessments": Thus, as recited in the 8 August 2006 order:

> *"The materials of the review[132] established that accounts of Yukos Capital S.a.r.l. ...had been used to amass financial resources acquired by illicit means. For example, in 2001-2003, oil belonging to Yuganskneftegaz OJSC, Samaraneftegaz OJSC and Tomskneft East Siberian Oil Company OJSC was transferred at unjustifiably undervalued prices to the balance sheets of dummy oil traders Fargoil LLC, Ratibor LLC and others, and then sold at market (world) prices for export and in the domestic market; the illicit proceeds amassed in the accounts of the aforesaid dummy Russian companies were transferred through a number of foreign companies to the accounts of Yukos Capital S.a.r.l.*
>
> *In this way, the oil-producing organizations of Yukos Oil Company OJSC were deprived illegally of the bulk of their profits, which was placed at the disposal of the oil company's directors and managers.*
>
> *Then, in connection with a lack of working capital, on the balance sheets of Yukos Oil Company OJSC and its oil-producing organizations and other subsidiaries, to finance their chartered economic activities, the funds were provided at certain interest rates under fraudulent loan agreements in which Yukos Capital S.a.r.l. played the role of lender."*

183. The next day, on 9 August 2006, a raid was conducted at the offices of Yukos Capital's Russian lawyers. All files pertaining to Yukos Capital were seized, as was the firm's central hard disk containing information on almost every case in which the firm was involved. The individual hard disks of every lawyer involved in the Yukos Capital case were also seized. No copies were left behind and the firm was essentially disabled from functioning.

---

131 Order of the Deputy Prosecutor General of the Russian Federation to Initiate a Criminal Case and Proceedings dated 8 August 2006 (Exhibit C75).

132 *See* p. 2. None of these "materials" was identified in the prosecutor general's order.

184. By decision dated 28 September 2006, Yukos Capital's appeal of the 19 July 2006 decision was suspended pending entry of a verdict in the criminal case instituted on 8 August.[133] The decision states in pertinent part as follows (emphasis added):

> *"The Court of Appeal has examined the order issued by R.A. Khatypov, the special investigator at the Prosecutor General's Office of the Russian Federation, by which proceedings were instituted in the criminal case No. 18/377465-06.....[i]n view of these circumstances and taking into consideration the fact that establishment [of] the authenticity of the information stated in the Loan Agreements Yu03-243/842 dated 2 December 2003 and No. 08-355 dated 19 August 2004 [i.e., the YO Loans] is of direct significance for establishing the validity of the claims by Yukos Capital S.a.r.l., since it is these agreements that serve as grounds for the claims filed in the proceeding, the Court of Appeal finds that the motion is justified and shall be sustained, and the proceedings in the matter of the appeal compliant filed by Yukos Capital S.a.r.l. against the ruling of the Arbitration Court of the city of Moscow dated 19 July 2006 in the case No. A40-11836/06-88-35 "B" regarding the bankruptcy of Yukos Oil Company OJSC shall be suspended until a sentence in the case No. 18/377465-06...enters into force."*[134] (emphasis added)

185. Thus, pursuant to the appeals' court order of 28 September 2006, Yukos Capital's appeal concerning its initial application to be included on the register of creditors was stayed. More importantly for purposes of this case, the ground for granting the stay was that the criminal case might determine the validity of the Government's claim that the Loans were invalid. Two further points require mention. First, the 28 September 2006 ruling recognised that no court had determined the Loans to be invalid (in any respect). Second, the criminal case against Yukos Capital was never pursued, being utterly devoid of merit.

186. In light of the commencement of formal bankruptcy proceedings against Yukos, on or about 6 October 2006, Yukos Capital filed a second application for inclusion of the Loan claims in the Registry of Claims.[135] In this application, Yukos Capital noted that any question concerning whether Yukos Oil's obligations under the loans were

---

[133] Ruling of the Ninth Arbitration Court of Appeal dated 28 September 2006 (Exhibit C76).

[134] *Ibid* pp. 2 and 3.

[135] Application for Inclusion of a Claim by Yukos Capital S.a.r.l. in the Registry of Claims of Creditors of Yukos Oil Company OJSC dated 6 October 2006 (Exhibit C77).

currently due and owing (the principal grounds for the court's 19 July 2006 decision) had been eliminated by the commencement of formal bankruptcy proceedings:

> *"Pursuant to Article 126 of the Federal Law on Insolvency (Bankruptcy), the date on which an arbitration court issues a judgment declaring a debtor bankrupt and initiating bankruptcy proceedings is also deemed to be the date on which financial obligations of the debtor that arose prior to the initiation of bankruptcy proceedings and mandatory payments owed by the debtor become due."*[136]

187. As noted above, and as set forth in Yukos Capital's 6 October 2006 application, the amounts due under the Loans were as follows (as of that date):

<u>December 2003 Loan</u>:	RUR 79.3 billion (USD 2.95 billion)[137] in principal RUR 14.9 billion (USD 0.55 billion) in interest
<u>August 2004 Loan</u>:	RUR 9.5 billion (USD 355 million) in principal RUR 971 million (USD 36.2 million) in interest
<u>Late repayment penalty:</u>	RUR 23.5 billion (USD 0.87 billion)

188. Submissions in opposition to Yukos Capital's second application to register its claims as a creditor were made by Rebgun and the Russian Federal Tax Service.[138] These submissions were not provided to Yukos Capital in advance of the hearing, in violation of Russian law. Yukos Capital's counsel also came to the conclusion that she could not attend the hearing on the application as a result of improper pressure from the Prosecutor General's office. Among other things, in addition to the police raids on counsel's office and the seizure of files, threats were made to initiate a prosecution against her son in connection with his entirely unrelated business. As discussed below, the court nonetheless determined to proceed with the matter.

189. In his *ex parte* submission, Rebgun took the position that the second application raised the same issues that were already the subject of the first application (and Yukos Capital's appeal from the denial of that application) and the criminal proceedings.

---

136 *Ibid* ¶ 15.

137 Based on the exchange rate of RUR/USD of 26.8197/1 as reported by the Central bank of Russia on 1 August 2006.

138 *See* Comments concerning the claims of Yukos Capital S.a.r.l. of 11 October 2006 (Exhibit C78) and Petition of the Receiver of Yukos Oil Company OJSC dated 23 November 2006 (Exhibit C80).

Accordingly, Rebgun submitted that this constituted grounds for dismissing the second application.

190. The submission by the Federal Tax Service was more extensive. The Tax Service argued again that there was no obligation of early repayment and thus no delinquent debt (and questioned again whether the November 2005 default notice had been sent), notwithstanding that the notion of delinquent debt had become legally irrelevant upon commencement of formal bankruptcy proceedings. Perhaps recognising this, the Tax Service submission went on as follows (in pertinent part) (emphasis added):

> *"Moreover, the court has already concluded that the debtor itself, through YUKOS Capital S.a.r.l., is attempting to include in the creditors' registry of claims for loans that are essentially the funds of Yukos Oil Company OJSC itself. Apart from the evidence examined by the court, the latter fact is confirmed by the financial reorganization plan submitted by the debtor for Yukos Oil Company OJSC.*
>
> *Insofar as the $14 billion in internal corporate claims ('claims of current Yukos subsidiaries' – point G, section 1, Claims Against Yukos, of the Financial Reorganization Plan) referred to in the reorganization plan are indeed claims filed by YUKOS Capital S.a.r.l. – claims that the latter will forego at the debtor's request – one would be justified in concluding that in effect Yukos Oil Company OJSC, through the loan agreements, was reserving its own funds that had previously been placed in offshore zones under the tax evasion schemes that were being used. For example, in one of the cases involving the assessment of additional taxes, penalty and fines on Yukos Oil Company OJSC, the arbitration court came to the conclusion that 'the financial resources in Yukos Oil Company OJSC's Fund (the Financial Support Fund for Production Development, which amassed funds from taxes never paid by 'dummy companies') were used to pay dividends to shareholders' (p. 30 of the Ninth Arbitration Court of Appeal's ruling of 5 March 2005 in Case No. 09AP-424/05-AK).*
>
> *Furthermore, the Court has already concluded that 'for all practical purposes, Yukos Oil Company OJSC reserved its own funds for settling the claims of the tax authorities.' First, the court has already examined evidence submitted by the tax service indicating that the executive board of Yukos Oil Company OJSC decided to comply in full with the court judgment regarding its tax liability for 2000. Second, given the totality of the evidence in the case:*
>
> -- *the application of YUKOS Capital S.a.r.l. for inclusion in the registry of creditors' claims of 27 April 2006 (p. 2, Volume 449);*

-- *the explanatory memorandum of Yukos Oil Company OJSC regarding its 2005 records, which was submitted to the tax authority on 15 May 2006 (pp. 2-47, Volume 1022); and*

-- *the letter from the president of Yukos Oil Company OJSC of 12 July 2006 (p. 1, Volume 1022),*

the court's conclusion as to the origin of the funds is consistent with the circumstances of the case."[139]

191. Putting it more concisely, the submission of the Federal Tax Service was that (i) the court had in prior decisions already found that the funds loaned by Yukos Capital were Yukos Oil's own funds and (ii) this finding was properly inferred from the facts that (a) Yukos Oil did not in its May 2006 accounting to the tax authorities list as "current" obligations the debt to Yukos Capital, (b) it was only mentioned in a letter from Yukos' CEO after Yukos Oil had been placed under bankruptcy supervision and (c) it was said in the reorganisation plan proposed by Yukos Oil that the debt could be ignored.

192. The Federal Tax Service was wrong, misleadingly so, on all counts: the court had not considered or decided the issue of the ownership of loan proceeds, but merely cited the order of the prosecutor general's office commencing criminal proceedings (which in turn relied on a report of the Federal Tax Service itself) as grounds for suspending proceedings. Indeed, in its 28 September 2006 decision, the appellate court emphasised that "*establishing the veracity of the information set forth in Loan Agreements No. Yu03-243/842 of 2 December 2003 and No. 08-355 of 19 August 2004 [i.e., the YO Loans] is of direct significance to establishing the validity of Yukos Capital S.a.r.l.'s claims."* That is, the correctness of the Federal Tax Service's allegations had not been established and, by necessary implication, Yukos Capital's claims could not be denied unless and until it was.

193. It is of some interest that the Federal Tax Service failed to submit as evidence any of the alleged "materials" underlying its report on which the prosecutor had relied (or been told to rely). It instead cited three documents which, neither singly nor together, say anything about ownership of the funds loaned to Yukos Oil.

139 Exhibit C78, pp. 1 and 2.

194. The hearing on Yukos Capital's second application to register its claims took place on 27 November 2006.[140] As noted above, no representative of Yukos Capital appeared for the hearing, but the court determined to proceed in Yukos Capital's absence "*since the latter had been notified of the time and place of the proceeding.*" This determination was made despite Yukos Capital having made the court aware of the reason for counsel's non-appearance (*i.e.*, improper threats directed at counsel and her son). At the conclusion of the hearing, the court issued an oral decision denying Yukos Capital's application.

195. The court's written decision was issued on or about 4 December 2006.[141] Therein, the court rejected Rebgun's argument that the application should be dismissed as already the subject of pending proceedings. The arguments of the Federal Tax Service, on the other hand, were accepted in full. Indeed, the bulk of the court's written decision repeats verbatim the Federal Tax Service's submission in opposition to the application (quoted above).

196. Yukos Capital filed an appeal of the 4 December 2006 decision with the Ninth Arbitration Court of Appeal.[142] In its appeal, Yukos Capital emphasised that it had not received any objection to its claim and, if evidence had been presented at the hearing itself absent prior notice or disclosure, Russian law required that it not be considered by the court. Yukos Capital also noted that, in any event, matters concerning the delinquency of the Loans were irrelevant and that, properly considered:

> *"Basing on the provisions of the civil legislation of the Russian Federation (Chapter 42 of the Civil Code of the Russian Federation), governing the legal relationships between the parties under a contract of loan and the extensive judicial practice of their application, the following facts are of importance when examining the Creditor's claim to debtor: an event of the actual loan granting in the requested sum and the fact of the maturity date of the obligations relating to the refund of the loan. Both facts, specified above, have been confirmed by the Applicant and they have not been denied by the Court*

---

[140] Record of Court Proceedings of the Moscow City Arbitration Court dated 27 November 2006 (Exhibit C81).

[141] Decision of the Moscow City Arbitration Court of 27 November 2006 (4 December 2006) (Exhibit C82).

[142] *See* Appeal of Yukos Capital S.a.r.l. against the Decision of the Moscow Arbitration Court as of 4 December 2006 (Exhibit C83).

> *(moreover, the Court has not even examined these issues in the appealed Decision).*
>
> * * *
>
> *The mentioned conclusions of the Court do not have and cannot have a legal basis (and the Court has stated no legal norms) as far as a parent company and a subsidiary company appear to be separate and independent subjects of civil legal relationships in accordance with the civil legislation of the Russian Federation, which can close and perform any transactions including those between each other. At the same time, conclusion of a transaction between the dependent persons does not form a basis for non-performance of the obligations under such transaction."*[143]

197. With respect to ownership of loan proceeds, Yukos Capital added:

> *"If such issues had entered into the subject of proof under the present case then in such case the evidence, quoted in the Decision of the Court, would not confirm (even in an indirect form) the fact that the monetary funds, granted by the Applicant to the debtor as a loan, have been obtained from [Yukos Oil] in an illegal way."*[144]

Yukos Capital concluded by noting:

> *"In case the matter is in the validity of the given contracts (although the Court has not brought up such a question) then the Civil Code of the Russian Federation provides for enough legal measures and establishes a certain procedure for the acknowledgement of transactions as invalid. However, as it has been mentioned before, no one has submitted a claim to nullify the examined contracts of loan."*[145]

198. A hearing on the appeal was held on 17 January 2007. Representatives of Yukos Capital again did not appear for the reasons discussed previously and the court postponed the hearing to 15 February 2007. Yukos Capital did not appear on the postponed date and the hearing was held in its absence. The court issued an oral decision dismissing the appeal, with a written decision to follow.

---

143 *Ibid* ¶¶ 18.1, and 18.5.

144 *Ibid* ¶ 18.3.

145 *Ibid* ¶ 18.6.

199. The court's written decision was issued on or about 22 February 2007[146]. Therein, the court held that the lower court had "*established that the debtor, through Yukos Capital S.a.r.l., was attempting to include in the creditors' registry claims for loans that were essentially the funds of Yukos Oil Company OJSC itself.*"[147] The appellate court repeated, again almost verbatim, the relevant part of the 4 December 2006 decision on this point which itself had, as noted previously, adopted verbatim the incorrect and misleading text of the Federal Tax Service's untimely *ex parte* opposition to Yukos Capital's application to register its claims. In light of the above, the appellate court held that:

> *"Given these circumstances, the lower court rightly concluded that the sum total of Yukos Oil Company OJSC's actions confirmed the validity of the court's earlier conclusion that the loans were, in effect, funds of the debtor itself received for the payment of tax liability."*[148]

200. Yukos Capital timely filed a cassation appeal from the 22 February 2007 decision[149].

201. On or about 17 May 2007, Rebgun commenced proceedings to invalidate the Loans[150]. At about the same time, Rebgun filed a motion to suspend Yukos Capital's two cassation appeals (*i.e.*, its appeals of the courts' decisions denying the registration of its claims).[151] As alleged in the motion, consideration of the cassation appeals would be impossible pending resolution of the new invalidation proceedings because *"the possible invalidation of the loan agreements could deprive Yukos Capital S.a.r.l. of grounds for filing claims pursuant to the Federal Law on Insolvency (Bankruptcy)."*[152] Rebgun was correct in his assessment that the "possible" invalidation of the Loan agreements might deprive Yukos Capital of grounds to file claims in the Yukos bankruptcy. Significantly, however, the implication of this statement, also undeniably correct, was that the Loans had not been invalidated, an

---

146 Judgment of the Ninth Arbitration Court of Appeal dated 22 February 2007 (Exhibit C84).

147 *Ibid* p. 2.

148 *Ibid* p. 3.

149 *See* Cassation Appeal by Yukos Capital S.a.r.l. of the 4 December 2006 Decision of the Moscow Arbitration Court (10 April 2007) (Exhibit C85).

150 Petition of the Receiver of Yukos Oil Company OJSC to have the Loan Agreement Ruled Invalid dated 17 May 2007 (Exhibit C86).

151 *See* Motion for Suspension of Proceedings in Cassation Appeal filed by the Receiver of Yukos Oil Company OJSC dated 24 May 2007 (Exhibit C87).

152 *Ibid* p. 2.

implication flatly inconsistent with the prior positions taken by the Federal Tax Service and adopted by the courts in denying Yukos Capital's second application to include its claims in the bankruptcy. By decisions dated 31 May and 20 July 2007, Yukos Capital's cassation appeals were suspended[153].

202. As discussed above, the Yukos bankruptcy was concluded in November 2007. With the conclusion of the bankruptcy, and dissolution of Yukos, the Russian courts terminated both (i) Yukos Capital's appeals from the decisions denying its applications to participate as a creditor in the Yukos bankruptcy[154] and (ii) Rebgun's proceedings to invalidate the Loans.

203. Claimant's efforts to participate as a creditor in the Yukos bankruptcy, in which all registered creditors were paid in full, may thus be summarised as follows:

- Yukos Capital's initial application was denied on the basis that the Loans were not yet due, a decision in direct conflict with the evidence and, like all relevant decisions in this matter, one where the court simply adopted verbatim the submissions of the Russian tax authorities;

- Yukos Capital's second application was not opposed by anyone until the very day of the hearing. Submissions were then made by Rosneft, Rebgun and the tax authorities in circumstances where it was known Yukos Capital would have no opportunity to respond because its counsel had been threatened and made to stay away;

- Despite Yukos Capital's absence from the hearing and despite the fact that no objection to its claim had been timely submitted, the court proceeded with the hearing and, in rejecting Yukos Capital's claim, adopted verbatim the submission of the Russian tax authorities;

- The submission of the tax authorities was demonstrably wrong and intentionally misleading in that (i) no court had ever found the funds loaned to Yukos Oil to have been its own (nor could it) and (ii) the three documents relied upon by the tax authorities can in no way support that proposition, much less prove it;

---

153 *See* Decision of the Moscow District Federal Arbitration Court of 24 May 2007 (31 May 2007) (No. KG-A40/4522-07) (Exhibit C88) and Decision of the Moscow District Federal Arbitration Court dated 20 July 2007 (No. A40-11836/06-88-35) (Exhibit C90).

154 Determination of the Federal Arbitration Court of the Moscow District (No. KG-A40/3637-08) dated 8 May 2008 (Exhibit C101).

- The court's decision rejecting Yukos Capital's claim was upheld on appeal without any critical analysis whatsoever and with the appellate court again adopting the submissions of agents of the Russian State;

- In a tactic designed to delay any further appeals by Yukos Capital while the Yukos bankruptcy was completed, Rebgun commenced meritless proceedings to invalidate the Loans (thus unwittingly contradicting the purported basis on which the tax authorities and the courts had rejected Yukos Capital's claim); and

- When the bankruptcy was completed, Rebgun and the courts used that as the basis to terminate and discontinue Yukos Capital's suspended appeals.

204. Only one conclusion may be drawn—whether coerced or complicit, the Russian courts' rulings rejecting Yukos Capital's application to participate as a creditor in the Yukos bankruptcy, in light of the evidence put before the courts, were arbitrary, capricious and contrary to due process and the rule of law. The effect, denying Yukos Capital its last route to recover on the Loans, was to expropriate Yukos Capital's Investments.

205. The Dutch courts reached the same conclusion in connection with similar loans made by Yukos Capital to YNG in 2004 (*i.e.*, around the same time as its Loans were made to Yukos Oil). Following Rosneft's "acquisition" of YNG, Yukos Capital sought to enforce those loans against YNG in arbitration proceedings brought in Moscow. Yukos Capital succeeded only to have the awards declared invalid by the Russian courts in proceedings brought by Rosneft.

206. Pursuant to a judgment of the Amsterdam Court of Appeal dated 28 April 2009, the Dutch courts held that the arbitration awards against YNG were enforceable in the Netherlands notwithstanding the decisions of the Russian courts. Among other things, the Amsterdam Court of Appeal found that:

> "*Rosneft has insufficiently rebutted that the Russian judiciary in cases that pertain to the (former) Yukos group (or parts thereof) or the (former) directors thereof and which concern interests that the Russian state considers to be its own, is not impartial and independent, but allows itself to be led by the interests of the Russian state and is instructed by the executive.*
>
> * * *
>
> *Rosneft has not asserted any concrete facts or submitted documents and nor have circumstances otherwise been shown that cast a*

> *different light on the influence of the Russian state on the Russian judiciary in the matter at hand.*
>
> * * *
>
> *[T]he judgments of the Russian civil court in which the arbitral awards were set aside were the result of a judicial process that must be qualified as partial and dependent, that these judgments cannot be recognized in the Netherlands. This means that in the assessment of the request by Yukos Capital to enforce the arbitral awards, the setting aside of these decisions by the Russian court must be ignored*".[155]

207. Standing in stark contrast to the treatment received by Yukos Capital is that given to other former Yukos affiliates which had come under the control of Rosneft and therefore the Russian State. Their claims (*e.g.*, the YNG "*mismanagement*" claim) were rubber stamped by the courts and paid in full.

VIII. YUKOS CAPITAL'S CLAIMS AND REQUESTS FOR RELIEF

A. Claimant's Principal Claim

208. The Russian State's dismantling and destruction of Yukos Oil as described herein, by acts attributable to it and in violation of international law, rendered the value of Claimant's Investments (*i.e.*, its Loans to Yukos Oil) nil. This constitutes the expropriation, or use of measures having effect equivalent to expropriation, of Claimant's Investments. Further, this expropriation was not in the public interest, was discriminatory, was not carried out under due process of law and was not accompanied by the payment of prompt, adequate and effective compensation. Accordingly, the Respondent has breached its obligations under Article 13(1) of the ECT.

209. The Russian State's dismantling and destruction of Yukos Oil, and consequent expropriation of Claimant's Investments, constitutes a breach of the Respondent's obligations under ECT Article 10(1) to: (i) create stable, equitable, favourable and transparent conditions for investors; (ii) accord fair and equitable treatment; (iii) provide constant protection and security; (iv) provide treatment no less favourable

155 Decision of the Amsterdam Court of Appeal dated 28 April 2009 in *Yukos Capital S.A.R.L. v. OAO Rosneft*, Case No. 200.005.269/01, ¶¶ 3.9.3, 3.10 (Exhibit C105).

than that required by international law; and (v) not impair by unreasonable or discriminatory measures the maintenance, use, enjoyment or disposal of investments.

210. The Russian State's dismantling and destruction of Yukos Oil, and consequent expropriation of Claimant's Investments, constitutes a breach of the Respondent's obligations under ECT Articles 10(2), (3) and (7) to accord investors treatment which is no less favourable to that accorded to other investors, whether its own, of any other Contracting Party to the ECT or any third state.

B. <u>Claimant's Alternative Claim</u>

211. In the alternative, the Russian State's rejection of Yukos Capital's claim to participate as a creditor in the Yukos bankruptcy as described herein, by acts attributable to it and in violation of international law, rendered the value of Claimant's Investments nil. This constitutes the expropriation, or use of measures having effect equivalent to expropriation, of Claimant's Investments. Further, this expropriation was not in the public interest, was discriminatory, was not carried out under due process of law and was not accompanied by the payment of prompt, adequate and effective compensation. Accordingly, the Respondent has breached its obligations under Article 13(1) of the ECT.

212. The Russian State's rejection of Yukos Capital's claim to participate as a creditor in the Yukos bankruptcy constitutes a breach of the Respondent's obligations under ECT Article 10(1) to: (i) create stable, equitable, favourable and transparent conditions for investors; (ii) accord fair and equitable treatment; (iii) provide constant protection and security; (iv) provide treatment no less favourable than that required by international law; and (v) not impair by unreasonable or discriminatory measures the maintenance, use, enjoyment or disposal of investments.

213. The Russian State's rejection of Yukos Capital's claim to participate as a creditor in the Yukos bankruptcy constitutes a breach of the Respondent's obligations under ECT Articles 10(2), (3) and (7) to accord investors treatment which is no less favourable to that accorded to other investors, whether its own, of any other Contracting Party to the ECT or any third state.

214. The Russian State's rejection of Yukos Capital's claim to participate as a creditor in the Yukos bankruptcy constitutes a breach of the Respondent's obligations under ECT

Article 10(12) to ensure the effective means for the assertion of claims and the enforcement of rights.

C. Yukos Capital's Request for Relief

215. Yukos Capital respectfully requests an Award:

(a) compensating it in an amount to be determined but not less than

(i) the RUR 80 billion principal amount of the December 2003 Agreement, together with accrued interest and penalty interest (RUR 270.6 billion through 31 January 2013) (*i.e.*, a total of USD 11.67 billion through 31 January 2013);[156] and

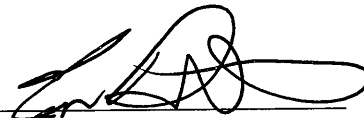
(ii) the USD 355 million principal amount of the August 2004 Agreement, together with accrued interest and penalty interest (USD 1.07 billion through 31 January 2013) (*i.e.*, a total of USD 1.4 billion through 31 January 2013);

(b) reimbursing its arbitration costs, including attorneys' fees; and

(c) for such other relief as the Tribunal may deem warranted.

Dated: 15 February 2013

Respectfully submitted,



Cyrus Benson
Osma Hudda
Victoria Barnes
Gibson, Dunn & Crutcher LLP
Telephone House
2-4 Temple Avenue
London EC4Y 0HB
UK

156 Based on the RUR/USD exchange rate of 30.0277/1 reported on 31 January 2013 by the Central Bank of Russia.

Laurence Shore
Lindsey D. Schmitd
Gibson, Dunn & Crutcher LLP
200 Park Avenue
New York, New York 10166-0193
USA