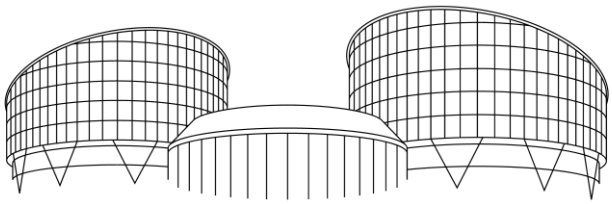

EUROPEAN COURT OF HUMAN RIGHTS
COUR EUROPÉENNE DES DROITS DE L'HOMME

FORMER FIRST SECTION

CASE OF OAO NEFTYANAYA KOMPANIYA YUKOS v. RUSSIA

(Application no. 14902/04)

JUDGMENT

This judgment was rectified on 17 January 2012
under Rule 81 of the Rules of Court

STRASBOURG

20 September 2011

FINAL

08/03/2012

This judgment has become final under Article 44 § 2 of the Convention. It may be subject to editorial revision.

In the case of OAO Neftyanaya Kompaniya Yukos v. Russia,

The European Court of Human Rights (First Section), sitting as a Chamber composed of:

Christos Rozakis, *President*,
Nina Vajić,
Khanlar Hajiyev,
Dean Spielmann,
Sverre Erik Jebens,
Giorgio Malinverni, *judges*,
Andrey Bushev, ad hoc *judge*,
and Søren Nielsen, *Section Registrar*,

Having deliberated in private on 24 June 2011,

Delivers the following judgment, which was adopted on that date:

PROCEDURE

1. The case originated in an application (no. 14902/04) against the Russian Federation lodged with the Court under Article 34 of the Convention for the Protection of Human Rights and Fundamental Freedoms ("the Convention") by OAO Neftyanaya Kompaniya Yukos ("the applicant company"), on 23 April 2004.

2. The applicant was represented by Mr P. Gardner, a lawyer practising in London. The Russian Government ("the Government") were initially represented by Mr P. Laptev and Ms V. Milinchuk, former Representatives of the Russian Federation at the European Court of Human Rights, and subsequently by their Representative, Mr G. Matyushkin.

3. By a decision of 29 January 2009, the Court declared the application partly admissible.

4. The applicant and the Government each filed further written observations (Rule 59 § 1).

5. A hearing took place in public in the Human Rights Building, Strasbourg, on 4 March 2010 (Rule 59 § 3).

There appeared before the Court:

(a) *for the Government*
Mr G. MATYUSHKIN, *Agent*,
Mr M. SWAINSTON QC,
Mr T. BRENNAN QC,
Ms M. LESTER,
Mr S. MIDWINTER,
Mr P. WRIGHT,
Mr Kh. IVANYAN,
Mr V. STARZHENETSKIY,
Ms N. ELINA,
Ms O. SIROTKINA
Ms O. YURCHENKO,
Ms E. KUDELICH,
Ms I. KOGANOVA,
Ms D. OBYSKALOVA,
Mr G. ABATOUROV,
Mr I. PLYUSHKOV,
Ms V. UTKINA,
Mr O. OVCHAR,
Ms T. STRUCHKOVA,
Mr D. MIKHAYLOV,
Mr V. TORKANOVSKIY,
Ms E. FILATOVA, *Advisers*;

(b) *for the applicant*
Mr P. GARDNER, *Counsel*.

The Court heard addresses by Mr Gardner, Mr Matyushkin and Mr Swainston QC, as well as the answers by Mr Gardner and Mr Swainston QC to questions put to the parties.

THE FACTS

I. THE CIRCUMSTANCES OF THE CASE

6. The applicant, OAO Neftyanaya Kompaniya YUKOS, was a publicly-traded private open joint-stock company incorporated under the laws of Russia. It was registered in Nefteyugansk, the Khanty-Mansi Autonomous

Region, and at the relevant time was managed by its subsidiary, OOO "YUKOS" Moskva, registered in Moscow.

7. The applicant was a holding company established by the Russian Government in 1993 to own and control a number of stand-alone entities specialised in oil production. The company remained fully State-owned until 1995-1996 when, through a series of tenders and auctions, it was privatised.

A. Proceedings in respect of the applicant company's tax liability for the year 2000

1. Tax assessment 2000

(a) Original tax inspection

8. Between 13 November 2002 and 4 March 2003 the Tax Inspectorate of the town of Nefteyugansk ("the Tax Office") conducted a tax inspection of the applicant company.

9. As a result of the inspection, on 28 April 2003 the Tax Office drew up a report indicating a number of relatively minor errors in the company's tax returns and served it on the company.

10. Following the company's objections, on 9 June 2003 the Tax Office adopted a decision in which it found the company liable for having filed incomplete returns in respect of certain taxes.

11. The decision of the Tax Office was accepted and complied with by the company on 7 July 2003.

(b) Additional tax inspection

12. On 8 December 2003 the Tax Ministry ("the Ministry"), acting as a reviewing body within the meaning of section 87 (3) of the Tax Code, carried out an additional tax inspection of the applicant company.

13. On 29 December 2003 the Ministry issued a report indicating that the applicant company had a large tax liability for the year 2000. The detailed report came to over 70 pages and had 284 supporting documents in annex. The report was served on the applicant company on the same date.

14. The Ministry established that in 2000 the applicant company had carried out its activities through a network of 22 trading companies registered in low-tax areas of Russia ("the Republic of Mordoviya, the town of Sarov in the Nizhniy Novgorod Region, the Republic of Kalmykiya, the town of Trekhgornyy in the Chelyabinsk Region, the town of Lesnoy in the Sverdlovsk Region and the Evenk Autonomous District"). For all legal purposes, most of these entities were set up as entirely independent from the applicant, i.e. as belonging and being controlled by third persons, although

their sole activity consisted of commissioning the applicant company to buy crude oil on their behalf from the company's own oil-producing subsidiaries and either putting it up for sale on the domestic market or abroad, or first handing it over to the company's own oil-processing plants and then selling it. There were no real cash transactions between the applicant company, its oil-processing and oil-producing subsidiaries and the trading entities, and the company's own promissory notes and mutual offsetting were used instead. All the money thus accumulated from sales was then transferred unilaterally to the "Fund for Financial Support of the Production Development of OAO Neftyanaya Kompaniya YUKOS", a commercial entity founded, owned and run by the applicant company. Since at all relevant times the applicant company took part in all of the transactions of the trading companies, but acted as the companies' agent and never as an owner of the goods produced and processed by its own subsidiaries and since the compensation paid by the trading entities for its services was negligible, the applicant company's real turnover was never reflected in any tax documents and, consequently, in its tax returns. In addition, most of the trading companies were in fact sham entities, as they were neither present nor operated in the place of their registration. In addition, they had no assets and no employees of their own.

15. The Ministry found it established, among other things, that:

(a) the actual movement of the traded oil was from the applicant company's production sites to its own processing or storage facilities;

(b) the applicant company acted as an exporter of goods for the purpose of customs clearance, even though the goods had formally been owned and sold by sham companies;

(c) through the use of various techniques, the applicant company indirectly established and, at all relevant times *de facto*, controlled and owned the sham entities;

(d) all accounting operations of the companies were carried out by the same two entities, OOO "YUKOS" FBC and OOO "YUKOS" Invest, both dependant on or belonging to the applicant company;

(e) the network of sham companies was officially managed by OOO "YUKOS" RM, all official correspondence, including tax documents, being sent from the postal address of OOO "YUKOS" Moskva, the applicant company's managing subsidiary;

(f) the sham companies and the applicant company's subsidiaries entered into transactions with lowered prices for the purpose of reducing the taxable base of their operations;

(g) all revenues perceived by the sham companies were thereafter unilaterally transferred to the applicant company;

(h) statements by the owners and directors of the trading entities, who confessed that they had signed documents that they had been required to sign by the officials of the applicant company, and had never conducted any independent activity on behalf of their companies, were true;

(i) and, lastly, that the sham companies received tax benefits unlawfully.

16. Having regard to all this, the Ministry decided that the activities of the sham companies served the purpose of screening the real business activity of the applicant company, that the transactions of these companies were sham and that it had been the applicant company, and not the sham entities, which conducted the transactions and became the owner of the traded goods. In view of the above, and also since neither the sham entities nor the applicant company qualified for the tax exemptions in question, the report concluded that the company, having acted in bad faith, had failed properly to reflect these transactions in its tax declarations, thus avoiding the payment of VAT, motorway tax, corporate property tax, tax for improvement of the housing stock and socio-cultural facilities, tax in respect of sales of fuels and lubricants and profit tax.

17. The report also noted specifically that the tax authorities had requested the applicant company to facilitate reciprocal tax inspections of several of its important subsidiaries. Five of the eleven subsidiary companies refused to comply, four failed to answer, whilst two entities filed incomplete documents. It also specified that during the on-site inspection the applicant company failed to provide the documents requested by the Ministry concerning the transportation of oil.

18. The report referred, *inter alia*, to Articles 7 (3), 38, 39 (1) and 41 of the Tax Code, section 3 of Law no. 1992-1 of the Russian Federation (RF) of 6 December 1991 "On Value-Added Tax", sections 4 and 5 (2) of RF Law no. 1759-1 of 18 October 1991 "On motorway funds in the Russian Federation", section 21 ("Ch") of RF Law no. 2118-1 of 27 December 1991 "On the basics of the tax system", Article 209 (1-2) of the Civil Code, section 2 of RF Law no. 2030-1 of 13 December 1991 "On corporate property tax", section 2 (1-2) of RF Law no. 2116-1 of 27 December 1991 "On corporate profit tax", Decision no. 138-O of the Constitutional Court of Russia of 25 July 2001 and Article 56 of the Tax Code.

19. On 12 January 2004 the applicant company filed its detailed thirty-page objections to the report. The company admitted that for a very short period of time it had partly owned three out of the twenty-two organisations mentioned in the report, but denied its involvement in the ownership and management of the remaining nineteen companies. They maintained this position about their lack of involvement in the companies in question throughout the proceedings.

20. During a meeting between the representatives of the Ministry and the company on 27 January 2004, the applicant company's counsel were given an opportunity to state orally their arguments against the report.

21. Having considered the company's objections, on 14 April 2004 the Ministry adopted a decision establishing that the applicant company had a large outstanding tax liability for the year 2000. As the applicant company had failed properly to declare the above-mentioned operations in its tax

declarations and to pay the corresponding taxes, in accordance with Article 122 (3) of the Tax Code the Ministry found that the company had underreported its tax liability for 2000 and ordered it to pay 47,989,241,953 Russian roubles ("RUB") (approximately 1,394,748,234 euros, ("EUR")) in tax arrears, RUB 32,190,599,501.40 (approximately EUR 935,580,142) in default interest and RUB 19,195,696,780 as a 40% penalty (approximately EUR 557,899,293), totalling RUB 99,375,538,234.40 (approximately EUR 2,888,227,669). The arguments contained in the decision were identical to those of the report of 29 December 2003. In addition, the decision responded in detail to each of the counter-arguments advanced by the company in its objections of 12 January 2004.

22. The decision was served on the applicant company on 15 April 2004.

23. The company was given until 16 April 2004 to pay voluntarily the amounts due.

24. The applicant company alleged that it had requested the Ministry to clarify the report of 29 December 2003 and that the Ministry had failed to respond to this request.

(c) Institution of proceedings by the Ministry

25. Under a rule which made it unnecessary to wait until the end of the grace period if there was evidence that the dispute between the tax authority and the taxpayer was insoluble, the Ministry did not wait until 16 April 2004.

26. On 14 April 2004 it applied to the Moscow City Commercial Court ("the City Court") and requested the court to attach the applicant company's assets as a security for the claim.

27. By decision of 15 April 2004 the City Court initiated proceedings and prohibited the applicant company from disposing of some of its assets pending the outcome of litigation. The injunction did not concern goods produced by the company and related cash transactions.

28. By the same decision the court fixed the date of the preliminary hearing for 7 May 2004 and invited the applicant company to respond to the Ministry's claims.

29. On 23 April 2004 the applicant company filed a motion in which it argued that the City Court had no territorial jurisdiction over the company's legal headquarters and requested that the case be referred to a court in Nefteyugansk, where it was registered.

30. On 6 May 2004 the Ministry filed a motion inviting the court to call the applicant company's managing subsidiary OOO "YUKOS" Moskva as a co-defendant in the case.

(d) Hearing of 7 May 2004

31. At the hearing the City Court examined and dismissed the applicant company's motion of 23 April 2004. Having regard to the fact that the

applicant company was operated by its own subsidiary OOO "YUKOS" Moskva, registered and located in Moscow, the court established that the applicant company's real headquarters were in Moscow and not in Nefteyugansk. In view of the above, the court concluded that it had jurisdiction to deal with the case.

32. On 17 May 2004 the applicant company appealed against this decision. The appeal was examined and dismissed by the Appeals Division of the Moscow City Commercial Court ("the Appeal Court") on 3 June 2004.

33. The City Court also examined and granted the Ministry's motion of 6 May 2004. The court ordered OOO "YUKOS" Moskva to join the proceedings as a co-defendant and adjourned the hearing until 14 May 2004.

34. At the hearing of 7 May 2004 the applicant company lodged with the City Court a separate action against the tax assessment of 14 April 2004, seeking to have the assessment decision declared unlawful. The applicant company's brief came to 42 pages and had 22 supporting documents in annex. This action was examined separately and dismissed as unsubstantiated by the City Court on 27 August 2004. The judgment of 27 August 2004 was upheld on appeal on 23 November 2004. On 30 December 2005 the Circuit Court upheld the decisions of the lower courts.

(e) Hearing of 14 May 2004

35. In the meantime the tax assessment case continued. On 14 May 2004 the City Court rejected the applicant company's request to adjourn the proceedings, having found that the applicant company's counterclaim did not require such adjournment of the proceedings concerning the Ministry's action.

36. OOO "YUKOS" Moskva also requested that the hearing be adjourned as, it claimed, it was not ready to participate in the proceedings.

37. This request was rejected by the court as unfounded on the same date.

38. At the hearing the respondent companies also requested the City Court to vary their procedural status to that of interested parties.

39. The court rejected this request and, on the applicant company's motion of 15 April 2004, ordered the Ministry to disclose its evidence. The company's motion contained a lengthy list of specific documents which, it alleged, should have been in the possession of the Ministry in support of its tax claims.

40. The court then decided that the merits of the case would be heard on 21 May 2004.

41. On 17 May 2004 the Ministry invited the applicant company to examine the evidence in the case file at its premises. Two company lawyers went to the Ministry on 18 May and four lawyers went on 19 May 2004.

42. According to the applicant company, the supporting material underlying the case was first provided to the company on 17 May 2004, when the Ministry filed approximately 24,000 pages of documents. On 18 May

2004 the Ministry allegedly disclosed approximately a further 45,000 pages, and a further 2,000 pages on the eve of the hearing before the City Court, that is, on 20 May 2004.

43. Relying on a record dated 18 May 2004[1], drawn up and signed by S. Pepelyaev and E. Aleynikova (Ministry representative A. Bondarev allegedly refused to sign it), the applicant company submitted that the documents in question had been presented in an indiscriminate fashion, in unpaginated and unsorted piles placed in nineteen plastic crates (ten of which contained six thousand pages each, with nine others containing some four thousand pages each). All of the documents were allegedly crammed in a room measuring three to four square metres, with two chairs and a desk. No toilet facilities or means of refreshment were provided.

44. According to the Government, the documents in question (42,269 pages - and not 45,000 pages as claimed by the applicant- filed on 18 May 2004, and a further 1,292 - and not 2,000 pages as claimed by the applicant company, filed on 20 May 2004) were well-known to the applicant company; moreover, it had already possessed these accounting and legal documents prior to the beginning of the proceedings. The documents allegedly reflected the relations between the applicant company and its network of sham entities, and the entirety of the management and accounting activities of these entities had been conducted by the applicant company from the premises of its executive body OOO Yukos-Moskva, located in Moscow. All of the documents were itemised in the Ministry's document dated 17 May 2004 and filed in execution of the court's order to disclose the evidence.

45. The Government also submitted that the applicant company's lawyers could have studied the evidence both in court and at the Ministry's premises throughout May, June and July 2004.

(f) First-instance judgment

46. The hearings on the merits of the case commenced on 21 May and lasted until 26 May 2004. It appears that the applicant company requested the court repeatedly to adjourn the proceedings, relying, among other things, on the lack of sufficient time to study the case file.

47. The Government submitted that the first day of the hearings, 21 May 2004, was devoted to hearing and resolving various motions brought by the applicant company and OOO Yukos-Moskva. On 24 May 2004, after hearing further motions by OOO Yukos-Moskva, the court proceeded to the evidence phase of the trial. The Tax Ministry then explained the evidence that it had submitted to the court. During this phase of the trial, which continued on 25 May 2004, the applicant company's representatives were able to ask questions, and the defendants made various motions. According to the

[1] Rectified on 17 January 2012 : the text was "18 May 2008"

Government, where the court found that the applicant company had not had an opportunity to review a particular document that the Ministry wished to refer to, the court refused to allow the document to be entered in the record. On 26 May 2004 the applicant company was afforded an opportunity to explain its evidence and to submit additional evidence. The applicant company chose instead to address questions to the Ministry. The applicant company concluded the first-instance hearing of the case with over three hours of pleadings, whilst the Ministry limited its pleadings to brief references to its own tax inspection report, the decision dated 14 April 2004 and the statement of claim.

48. On 26 May 2004, at the end of the hearings, the City Court gave its judgment in which, for the most part, it reached the same findings and came to the same conclusions as in the Ministry's decision of 14 April 2004. Having confirmed the factual findings of the decision of 14 April 2004 in respect of the relations and transactions between the sham companies and the applicant company with reference to sundry pieces of evidence, including the statements by the nominal owners of the trading companies, acknowledging to the true nature of their relations with the applicant company, the court then reasoned as follows:

> "... Under section 3 of RF Law no. 1992-1 of 6 December 1991 'On value-added tax', part 2 of section 5 and section 4 of RF Law no. 1759-1 of 18 October 1991 'On motorway funds in the Russian Federation', subpart 'ch' of section 21 of RF Law no. 2118-1 of 27 December 1991 'On the basics of the tax system', the sale of goods (works and services) gives rise to an obligation to pay VAT, motorway users' tax, tax on the sale of oil and oil products and tax for the maintenance of the housing stock and socio-cultural facilities.
>
> Under part 1 of Article 38 of the Tax Code, objects of taxation may consist of the sale of goods (works and services), assets, profit, value of sold goods (works and services) or other objects having value, quantity or physical characteristics on the presence of which the tax legislation bases the obligation to pay tax.
>
> Under part 1 of Article 39 of the Tax Code, sales are defined as the transfer of property rights in respect of goods. Under subpart 1 and 2 of Article 209 of the Civil Code (taking into account Article 11 of the Tax Code) the owner of goods is the person who has the rights of ownership, use and disposal of his property, that is, the person who is entitled to carry out at his own discretion in respect of this property any actions which are not against the law and other legal acts and do not breach the rights and protected interests of other persons ...
>
> The court established that the owner of the oil sold under contracts concluded with organisations registered in low-tax territories had been OAO Yukos. The respondents' arguments about the unlawfulness of the use of the notion of *de facto* owner (*фактический собственник*) on the basis that, according to Article 10 (3) and Article 8 (1) part 3 of the Civil Code ... there existed a presumption of good faith on the part of parties involved in civil-law transactions and that therefore the persons indicated as owners in the respective contracts should be regarded as the owners, are baseless, because the above-mentioned organisations never acquired any rights of

ownership, use and disposal in respect of oil and oil products (*поскольку прав владения, пользования и распоряжения нефтью и нефтепродуктами у данных организаций не возникало*).

OAO NK Yukos was therefore under an obligation to pay [the taxes], and this obligation has not been complied with in good time.

Article 41 of the Tax Code establishes that profit is an economic gain in monetary form or in kind, which is taken into account if it is possible to evaluate it and in so far as it can be assessed. Under subparts 1 and 2 of section 2 of RF Law no. 2116-1 of 27 December 1991 'On profit tax of enterprises and organisations' which was then in force, the object of taxation is the gross profit of the enterprise, decreased (or increased) in accordance with the provisions of the present section. The gross profit is the total of revenues (receipts) from the sale of products (works and services), main assets (including plots of land), other property belonging to the enterprise and the profit derived from operations other than sales, less the sum of expenses in respect of these operations. Since it follows from the case file that the economic profit from the sale of oil and oil products was perceived by OAO NK Yukos, it was incumbent on [the applicant company] to comply with the obligation to pay profit tax.

Section 2 of RF Law no. 2030-1 of 13 December 1991 'On corporate property tax' taxes the main assets, non-material assets, reserves and receipts which are indicated on the taxpayer's balance sheet. It follows that the obligation to pay property tax was incumbent on the person who was legally responsible for reflecting the main assets, non-material assets, reserves and receipts on its balance sheet. Since it follows from the materials of the case that OAO NK Yukos was under such an obligation, this taxpayer was also under an obligation to pay property tax.

The court does not accept the respondent's arguments that the tax authorities lacked the power to levy taxes from OAO NK Yukos in respect of the sums ... perceived by other organisations. The power of the tax authorities to bring proceedings in courts to ensure the payment of taxes to the budget in cases of bad-faith taxpayers is confirmed by decision no. 138-O of the Constitutional Court of the Russian Federation, dated 25 July 2001. At the same time the bad faith of taxpayer OAO NK Yukos and the fact that the proceeds from transactions in oil and oil products were remitted to it is confirmed by the materials of the case file.

The court has also established that the use of tax benefits by organisations which were dependent on OAO NK Yukos and participated in the tax-evasion scheme set up by that company was unlawful.

Pursuant to Article 56 of the Tax Code, tax benefits are recognised as preferences provided for in the tax legislation for certain groups of taxpayers in comparison with other taxpayers, including the possibility of not paying a tax or of paying it at a lower rate.

The court believes that tax payers must use their right to such benefits in good faith.

Meanwhile, it follows from the materials of the case that the taxpayers [concerned] used their right in bad faith.

The entities registered on the territory of the Republic of Mordoviya (OOO Yu-Mordoviya ..., ZAO Yukos-M ..., OAO Alta-Treyd ..., OOO Ratmir ..., OOO Mars

XXII ...) applied benefits governed by Law of the Republic of Mordoviya no. 9-Z of 9 March 1999 'On conditions for the efficient use of the socio-economic potential of the Republic of Mordoviya', which sets out a special taxation procedure for entities, for the purpose of creating beneficial conditions for attracting capital to the territory of the Republic of Mordoviya, developing the securities market and creating additional jobs. Under section 2 of that law, this special taxation procedure applies in respect of entities (including foreign entities operating through permanent representative offices established in the territory of the Republic of Mordoviya), established after the entry into force of the law (with the exception of entities conducting leasing activities, banks and other credit institutions) and whose business meets one of the following conditions: export operations, with the resulting quarterly earnings totalling at least 15% of the whole of the entity's earnings; wholesale trading of combustibles and lubricants and other kinds of hydrocarbons with the resulting quarterly earning totalling at least 70% of the whole of the entity's earnings; and other conditions enumerated in that law. Pursuant to sections 3 and 4 of the Law, the Government of the Republic of Mordoviya passed resolutions on the application of the special taxation procedure in respect of the mentioned entities and, consequently, on the application of the following tax rates: at the rate of 0% in respect of profit tax in so far as it is credited to the republican and local budgets of the Republic of Mordoviya; at the rate of 0% on motorway users' tax in so far as it is credited to the Territorial Road Fund of the Republic of Mordoviya; and at the rate of 0% on corporate property tax. Moreover, the above-mentioned entities were exempted by local government resolutions from payment of tax for the maintenance of the housing stock and socio-cultural facilities.

However, the special taxation procedure is provided for [by this law] for the purposes of creating favourable conditions in order to attract capital to the territory of the Republic of Mordoviya, develop the securities market and create additional jobs. The entities which used those benefits did not actually carry out their activities on the territory of this subject of the Russian Federation, did not attract capital and did not facilitate the strengthening of the Republic's socio-economic potential, but, on the contrary, inflicted material damage through non-payment of taxes to the budget of the Republic, the local budget and the federal budget. Thus, the use of the tax benefits in respect of these entities was not aimed at improving the economy of the Republic of Mordoviya but pursued the aim of evading taxes on the production, refining and sales operations in respect of oil and oil products by OAO NK Yukos and is, as a consequence, unlawful.

The entity registered on the territory of the Republic of Kalmykiya (OOO Sibirskaya Transportnaya Kompaniya ...) did not pay profit tax, property tax, motorway users' tax, tax on the acquisition of vehicles and other taxes, under Law no. 12-P-3 of the Republic of Kalmykiya of 12 March 1999 'On tax benefits to enterprises investing in the economy of the Republic of Kalmykiya', which establishes advantages in respect of taxes and duties for the ... taxpayers that invest in the economy of the Republic of Kalmykiya and are registered as such enterprises with the Ministry of Investment Policy of the Republic of Kalmykiya. Moreover, the entity in question was exempt from the payment of local taxes and ... of profit tax to the consolidated budget.

At the same time, it follows from the presumption of good faith on the part of taxpayers (Decisions no. 138-O of the Constitutional Court of 25 July 2001, no. 4-O of 10 January 2002 and no. 108-O of 14 May 2002, Rulings of the Presidium of the Supreme Commercial Court no. 9408/00 dated 18 September 2001, no. 7374/01 of 18 June 2002, no. 6294/01 of 5 November 2002 and no. 11259/02 of 17 December

2002 and letter no. C5-5/уп-342 of the Deputy President of the Supreme Commercial Court of 17 April 2002) that, for the use of tax advantages to become lawful, the amount of advantages provided and the sum of investments made by the entity should be commensurate. Since the amounts of benefits declared for tax purposes by the above-mentioned entities and the sums of investment made are obviously not commensurate, application of the advantages is unlawful. The application of tax advantages by the given entity is not aimed at improving the economy of the Republic of Kalmykiya but pursues the aim of tax evasion by OAO NK Yukos in respect of the operations of production, refining and sales of oil and oil products and, consequently, is unlawful.

The entity registered in the closed administrative territorial formation ('ZATO') town of Sarov in the Nizhniy Novgorod Region (OOO Yuksar ...) concluded a tax agreement on the provision of tax concessions with the Sarov municipal administration. The granting of additional tax advantages on the territory of the Sarov ZATO (Federal Nuclear Centre) in 2000 was regulated by the norms of Articles 21 and 56 of the Tax Code, section 58 of Law no. 227-FZ of 31 December 1999 'On the federal budget for the year 2000', section 5 of Law no. 3297-1 'On closed administrative territorial formations' of 14 July 1992, Item 2 of Paragraph 30 of Decree no. 222 of the Russian Government of 13 March 2000 'On measures for implementation of the Federal Law 'On the Federal Budget for 2000' and Regulations 'On the investment zone of the town of Sarov', approved by a Resolution of the Sarov Duma on 30 December 1999. According to the tax agreement, the Sarov administration confers advantages in respect of taxes payable into the Sarov budget to the entity in question in the form of a reduction in the share of taxes and other compulsory payments to the budget, up to 25% of the sums due in VAT, property tax, tax on the sale of fuel and lubricants, motorway users' tax, tax on vehicle owners, tax on the acquisition of vehicles, profit tax, tax on operations with securities and excise duties; in exchange, the entity undertakes to participate in investment projects (programmes) implemented in the Sarov investment zone or with its participation, aimed at raising additional budget receipts and solving the problems of Sarov's socio-economic development by transferring quarterly at least 1% of the sum of the tax advantages.

At the same time, according to Paragraph 1 of section 5 of the Federal Law no. 3297-1 'On closed administrative territorial formations' of 17 July 1992, additional benefits on taxes and duties are granted by the appropriate local government authorities to entities registered as taxpayers with the authorities of the closed administrative territorial formations in compliance with the above-mentioned law. Entities possessing at least 90% of their capital assets and conducting at least 70% of their activities on the territories of the closed administrative territorial formations (including the requirement that at least 70% of the average number of employees on the payroll must be made up of persons who permanently reside on the territory of the formation in question and that at least 70% of the labour remuneration fund must be paid to employees who permanently reside on the territory of the formation in question) enjoy the right to obtain the benefits in question. Given that OOO Yuksar did not actually carry out any activity on the territory of Sarov, was not actually present on the territory of Sarov and that there were no assets and production facilities necessary for the procurement and storage of oil on the territory of Sarov, Nizhniy Novgorod Region, the given entity applied the tax advantages unlawfully.

Thus, the use of tax advantages by the given entity is not aimed at improving the economy of the Sarov ZATO but pursued the aimed of tax evasion by OAO NK

Yukos in respect of its obligation to pay taxes on production and refining operations and the sale of oil and oil products and is, consequently, unlawful.

Entities registered in the Trekhgornyy ZATO in the Chelyabinsk Region (OOO Kverkus ..., OOO Muskron ..., OOO Nortex ..., OOO Greis ... and OOO Virtus ...) concluded tax agreements with the administration of the town of Trekhgornyy, according to which entities were granted advantages in respect of profit tax, tax for the maintenance of the housing stock and socio-cultural facilities, property tax, land tax, tax on the sale of fuel and lubricants, motorway users' tax, tax on vehicle users, and tax on the acquisition of vehicles, provided that the entities remitted the sum of 5% of the total amount of tax advantages conferred, for implementation of the town's socio-economic programmes, to the Trekhgornyy administration... Reasoning from the contents and meaning of the tax agreements, it follows that their purpose was implementation of the particularly important socio-economic task of developing the educational, medical and housing spheres in the Trekhgornyy ZATO. At the same time, the sums which were transferred to the budget by the taxpayers in question were many times lower than the sums of the declared tax advantages (the sum of investments is around 0.006% of the sum of the advantages for each taxpayer). Thus, the investments made by the taxpayers did not influence the development of Trekhgornyy's economy. On the contrary, since the above-mentioned organisations did not in fact carry out any activities, were never located on the territory of Trekhgornyy, had no assets and none of the production facilities necessary to buy and store oil on the territory of Trekhgornyy, the application of tax advantages by the above-mentioned organisations is contrary to part 1 of section 5 of RF Law no. 3297-1 of 17 July 1992 'On closed administrative territorial formations'.

The organisations registered in the Lesnoy ZATO in the Sverdlovsk Region (OOO Mitra ..., OOO Vald-oyl ..., OOO Bizness-oyl ...) concluded tax agreements on the granting of a targeted tax concession under which organisations were granted the concession in respect of profit tax, land tax, tax on the sales of fuel and lubricants, motorway users' tax, vehicle users' tax, tax on the acquisition of vehicles, tax for the maintenance of the housing stock and socio-cultural facilities and property tax, whilst the organisations [in question] were under an obligation to transfer to ... the Lesnoy municipal administration sums amounting to 5% of the sums of the granted tax concessions, but no less than 6,000 roubles quarterly, for implementation of the town's socio-economic programmes. [However], the amounts received from the taxpayers are many times lower than the totals of the declared tax advantages. Accordingly, the investments made by the taxpayers did not influence the development of the economy of the town of Lesnoy because the above-mentioned organisations never carried out any activities on the territory of Lesnoy, were never in fact located on the territory of Lesnoy and had no assets and none of the production facilities required to sell and store oil on the territory of Lesnoy, [and thus] the application of the tax advantages in respect of the above-mentioned organisations is contrary to part 1 of section 5 of RF Law no. 3297-1 of 17 July 1992 'On closed administrative territorial formations'.

The organisation registered in the Evenk Autonomous District (OOO Petroleum-Treiding) without in fact carrying out any activity on the territory of the district in question and without in fact being located on the territory of the Evenk Autonomous District, abused its right granted by Law no. 108 of the Evenk Autonomous District of 24 September 1998 'On specific features of the tax system in the Evenk Autonomous District'. The mentioned organisation was registered in the given district solely for the purpose of acquiring the right to the tax concession that could be granted in the Evenk

> Autonomous District. The use of the tax benefits by the organisation in question is not aimed at strengthening of economy of the Evenk Autonomous District, but is instead aimed at tax evasion by OAO NK Yukos in respect of extraction and processing transactions and the sale of oil and oil products and is thus unlawful.
>
> Thus, the use of tax concessions by the above-mentioned organisations is not aimed at strengthening the economy of the regions in which they were registered but is aimed at evading the taxes due in respect of the operations of extraction and processing transactions and the sale of oil and oil products by OAO NK Yukos and is thus unlawful. ..."

49. The first-instance judgment also responded to the applicant company's submissions. As regards the argument that the Ministry's calculations were erroneous in that they led to double taxation and the failure to take account of the right to a refund of VAT for export operations, the court noted that, contrary to the applicant company's allegations, both the revenues and expenses of the sham entities had been taken into account by the Ministry so as to avoid double taxation. In addition, under Law no. 1992-1 of 6 December 1991 "On value-added tax", in order to claim a refund of the VAT paid during export operations a taxpayer had to justify the claim in accordance with a special procedure and the applicant company had failed to apply for a refund either in 2000 or at any later date. As to the argument that the Ministry's claim was time-barred, the court refuted it with reference to Article 113 of the Tax Code and Decision no. 138-O of the Constitutional Court of 21 July 2001. The court held that the rules on limitation periods were inapplicable in the case at issue as the applicant company had acted in bad faith. In response to the company's argument that the interdependency within the meaning of Article 20 of the Tax Code was only relevant for the purposes of price correction under Article 40 of the Code, the court observed that the interdependency of the sham companies and the applicant company was one of the circumstances on the basis of which the tax authorities had proved that the tax offence had been committed by the applicant company in bad faith.

50. Accordingly, by the judgment of 26 May 2004 the court upheld the decision of 14 April 2004, albeit slightly reducing the payable amounts by reference to the Ministry's failure to prove the relations of the applicant company with one of the entities mentioned in the decision of 14 April 2004. The court ordered the applicant company to pay RUB 47,989,073,311 (approximately EUR 1,375,080,541) in taxes, RUB 32,190,430,314 (approximately EUR 922,385,687) in default interest and RUB 19,195,606,923 (approximately EUR 550,031,575) in penalties, totalling RUB 99,375,110,548 (approximately EUR 2,847,497,802) and ordered its managing subsidiary OOO "YUKOS" Moskva to comply with this decision. The judgment could be appealed against by the parties within a thirty-day time-limit.

51. At the hearings of 21 to 26 May 2004 the applicant company and its managing subsidiary were represented by eight counsel. The reasoned copy

of the judgment of 26 May 2004 was produced and became available to the parties on 28 May 2004.

(g) Appeal proceedings

52. On 1 June 2004 OOO "YUKOS" Moskva filed an appeal against the judgment of 26 May 2004.

53. The Ministry appealed against the judgment on 2 June 2004.

54. On 4 June 2004 the Appeal Court listed the appeals of OOO "YUKOS" Moskva and the Ministry to be heard on 18 June 2004.

55. On 17 June 2004 the applicant company filed its appeal against the judgment of 26 May 2004. The brief came to 115 pages and contained 41 documents in annex. The company complained, in particular, that the time for filing an appeal had been unlawfully abridged, in breach of its rights to fair and adversarial proceedings, that the first-instance judgment was ungrounded and unlawful, that the evidence in the case was unlawful, that the first-instance court had erred in interpretation and application of the domestic law, in that it had lacked legal authority to "assign" the tax liabilities of one company to another, and that the court's interpretation of the legislation on tax concessions had been erroneous. The company also argued that the lower court had wrongly assessed the evidence in the case and had come to erroneous factual conclusions in respect of the relationships between the applicant company and the sham companies, that in any event some of the operations of the sham companies had been unrelated to the alleged tax evasion and that the respective sums should not be "assigned" to the applicant company, and also that the case should have been tried in the town of Nefteyugansk, where the company was registered.

56. The Government submitted that the applicant company attempted to delay the examination of the case by dispatching the appeal brief to an erroneous address. According to the applicant, the above allegation was unsubstantiated.

57. The appeal hearing in the case lasted from 18 to 29 June 2004.

58. At the beginning of the hearing on 18 June 2004 the applicant company requested the Appeal Court to adjourn the proceedings. The company considered that the hearing had been fixed for too early a date, before the expiry of the statutory time-limit for lodging appeals.

59. The court refused this request as unfounded.

60. At the hearings of 21 and 28 June 2004 the applicant company filed four supplements to its appeal. The company and its managing subsidiary were represented by ten counsel.

61. Under Article 268 of the Code of Commercial Court Procedure the court fully re-examined the case presented by the Ministry rather than simply reviewing the first-instance judgment.

62. At the end of the hearing of 29 June 2004 the court delivered its judgment, in which it reached largely similar findings and came to the same

conclusions as the first-instance judgment. The court dismissed the company's appeals as unfounded, but decided to alter the first-instance judgment in part. In particular, it declared the Ministry's claims in respect of VAT partly unfounded, reduced the amount of the VAT arrears by RUB 22,939,931 (approximately EUR 649,336) and quashed the corresponding penalty of RUB 10,334,226 (approximately EUR 292,520).

63. The court judgment, in its relevant parts, read as follows:

> "... The parties declared under part 5 of Article 268 of the Code of Commercial Courts Procedure that there was a need to verify the lawfulness and grounds of the first-instance judgment and to hold a fresh hearing of the case in full.
>
> The Appeal Court has checked the lawfulness and grounds of the first-instance judgment pursuant to ... Article 268 ... of the Code of Commercial Court Procedure. ...
>
> The Appeal Court does not accept the arguments of the respondents concerning erroneous interpretation and application of the norms of the substantive law by the first-instance court and concerning the factual incorrectness of that court's conclusions.
>
> [The court went on to review and confirm all factual findings made by the Ministry and the first-instance court in respect of the tax-evasion scheme set up by the applicant company.]
>
> ... Bearing in mind the above-mentioned circumstances, the Appeal Court has established that the *de facto* owner of the oil was [the applicant company]. The acquisition of the oil and its transfer and subsequent sale was in reality carried out by [the applicant company] as the owner, which is proved by the control of [the applicant company] over all operations, and the actual movement of the oil from the extracting entities to processing entities or oil facilities controlled by [the applicant company], which is proved by the materials of the case.
>
> ...
>
> The [applicant company's] ownership of the oil is confirmed by the interdependence of the contracting parties, by the control that [the applicant company] had over them, by the registration of the contracting parties on territories with a low-tax regime, by the lack of activities by these entities at their place of registration, by the fact that the accounting operations for these entities was carried out by OOO Yukos-Invest or OOO Yukos-FBC, companies officially dependant on [the applicant company], by the fact that the accounting for these entities was filed from the addresses of [the applicant company] and OOO Yukos-Moskva, by the fact that their bank accounts were opened in the same banks owned by [the applicant company], by the presence and character of commercial relations between [the applicant company] and the dependent entities, and by the use of promissory notes and mutual offsetting between them.
>
> ...
>
> Under the legislation then in force, such as section 3 of RF Law no. 1992-1 of 6 December 1991 'On value-added tax', part 2 of Section 5 and section 4 of RF Law no. 1759-1 of 18 October 1991 'On motorway funds in the Russian Federation', subpart 'ch' of section 21 of RF Law no. 2118-1 of 27 December 1991 'On the basics

of the tax system', the sale of goods (works and services) gives rise to an obligation to pay VAT, motorway users' tax, tax on the sale of oil and oil products and the tax for the maintenance of the housing stock and socio-cultural facilities.

Under part 1 of Article 39 of the Tax Code, sales are defined as the transfer of property rights in respect of goods. Under subpart 1 and 2 of Article 209 of the Civil Code (taking into account Article 11 of the Tax Code) the owner of goods is the person who has the rights of ownership, use and disposal of his property, that is, the person who is entitled to carry out at his own discretion in respect of this property any actions which are not against the law and other legal acts and do not breach the rights and protected interests of other persons...

It follows that the person who in fact has the rights of ownership, use and disposal of the property and who, in view of these rights, exercises in reality and at his discretion in respect of his property any actions, including transfers of property to other persons ... is the owner of this property.

Therefore, OAO NK Yukos, being the *de facto* owner of the oil, was under an obligation to pay [the taxes], which has not been complied with in good time.

As was previously established, Article 41 of the Tax Code sets out that profit is an economic gain in monetary form or in kind, which is taken into account if it is possible to evaluate it and in so far as it can be assessed, and determined in accordance with the chapters 'Taxes in respect of the profits of natural persons', 'Taxes in respect of the profits of organisations', and 'Taxes in respect of the capital profits' of the Tax Code of the Russian Federation. Under subparts 1 and 2 of section 2 of RF Law no. 2116-1 of 27 December 1991 'On profit tax of enterprises and organisations' which was then in force, the object of taxation is the gross profit of the enterprise, decreased (or increased) in accordance with the provisions of the present section. The gross profit is the total of revenues (receipts) from the sale of products (works and services), main assets (including land parcels), other property of the enterprise and the profit derived from operations other than sales, less the sum of expenses in respect of these operations. The court established that the economic profit from the sale of oil and oil products was perceived by OAO NK Yukos, [and] it was incumbent on [the applicant company] to comply with the obligation to pay profit tax.

Section 2 of RF Law no. 2030-1 of 13 December 1991 'On corporate property tax' taxes the main assets, non-material assets, reserves and receipts which are indicated on the taxpayer's balance sheet. It follows that the obligation to pay property tax was incumbent on the person who was legally responsible for reflecting the main assets, non-material assets, reserves and receipts on its balance sheet. Since it follows from the materials of the on-site tax inspection that OAO NK Yukos was under such an obligation, this taxpayer was also under an obligation to pay property tax.

The Constitutional Court of the RF in its decision of 25 July 2001 no. 138-0 stated that it followed from the meaning of the norm contained in part 7 of Article 3 of the Tax Code of the RF that there is a presumption of good faith on the part of taxpayers. In order to refute this and establish the taxpayer's bad faith, the tax authorities have the right – in order to strike a balance between public and private interests – to carry out necessary checks and bring subsequent claims in commercial courts in order to guarantee the payment of taxes to the budget.

In view of the above, the tax authorities ... have the right to carry out checks with a view to establishing the *de facto* owner of sold property and the *de facto* recipient of the economic profit, and also with a view to establishing [the owner's] bad faith as expressed in use of the tax-evasion scheme. At the same time, the tax authorities establish the *de facto* owner with regard to the actual relations between the parties to the transaction, irrespective of whether the persons were declared as owners of the property in the documents submitted during the tax inspections.

The circumstances indicating that OAO NK Yukos had in fact the rights of ownership, use and disposal of its oil and oil products and, at its discretion, carried out in this connection any actions, including the sale, transfer for processing, etc., through specially registered organisations dependant on OAO NK Yukos is confirmed by the materials of the case.

...

In view of the above, the court does not accept the respondent's arguments about the unlawfulness and the lack of factual basis of the decision to levy additional taxes from OAO NK Yukos as the *de facto* owner of the oil and oil products.

The respondent's argument that OAO NK Yukos had not perceived any economic profit from the application of benefits by the entities mentioned in the decision of the Ministry contradicts the materials of the case. The court had established that OAO NK Yukos received economic profit in the form of unilateral transfers of cash. OAO NK Yukos set up the Fund for Financial Support of the Production Development of OAO NK Yukos [to this end].

...

The argument of OAO NK Yukos that the Ministry is levying taxes in respect of transactions "within the same owner" is unsupported, since the calculations of additional taxes (except for the property tax in respect of which [this is inapplicable]) also take into account the expenses connected with the acquisition of the oil and oil products.

The court does not accept the respondent's arguments that the tax authorities lacked the power to levy taxes from OAO NK Yukos in respect of the sums ... perceived by other organisations. The power of the tax authorities to bring proceedings in courts to ensure the payment of taxes to the budget in cases of bad-faith taxpayers is confirmed by decision no. 138-O of the Constitutional Court of the Russian Federation, dated 25 July 2001. At the same time the bad faith of taxpayer OAO NK Yukos and the fact that the proceeds from transactions involving oil and oil products belonged to it is confirmed by the materials of the case file.

The circumstances of the ... acquisition and sale of the oil and oil products, taken in their entirety, as established by the Appeal Court, indicate the presence of bad faith in the actions of OAO NK Yukos, which was expressed in intentional actions aimed at tax evasion by the use of unlawful schemes. In accordance with part 2 of Article 110 of the Tax Code of the RF the tax offence is considered intentional if the person who has committed it knew about the unlawful character of the actions (inactions), wished them or knowingly accepted the possibility of the harmful consequences of such actions (inactions).

> Since OAO NK Yukos intentionally committed actions aimed at tax evasion, and its officers were aware of the unlawful character of such actions, wished or knowingly accepted the possibility of harmful consequences due to such actions, OAO NK Yukos must be held liable under part 3 of Article 122 of the RF Tax Code for the non-payment or incomplete payment of taxes due to the lowering of the taxable base or incorrect calculation of the tax or other unlawful actions (inactions) committed intentionally, in the form of a fine equivalent to 40% of the unpaid taxes.
>
> ...
>
> Having re-examined the case and verified the lawfulness and grounds of the first-instance judgment in full, having examined the evidence and having heard the arguments of the parties, the Appeal Court has come to the conclusion that the decision of the Ministry dated 14 April 2004 ... is in compliance with the Tax Code as well as with Federal laws and other laws on taxes...
>
> The claims for payment of taxes, interest surcharges and fines made in the decision of the Ministry of 14 April 2004 ... are grounded, lawful and confirmed by the primary documents of the materials of the inspection submitted in justification to the court. ..."

64. The appeal judgment also responded to the applicant company's other arguments. As regards the alleged breaches of procedure and the lack of time for the preparation of the defence at first instance, the court noted that it had examined this allegation and that there had been no violation of procedure at first instance and that, in any event, the applicant company had had ample opportunities to study the evidence relied on by the Ministry both at the Ministry's premises and in court. As regards the argument that the evidence used by the Ministry was inadmissible, the court noted that the materials of the case had been collected in full compliance with the requirements of the domestic legislation. The court also agreed with the first-instance court that the three-year statutory time-limit had been inapplicable in the applicant company's case since the company had been acting in bad faith.

65. The first-instance judgment, as upheld on appeal, came into force on 29 June 2004.

66. The applicant company had two months from the date of the delivery of the appeal judgment to challenge it in third-instance cassation proceedings (*кассация*).

(h) Cassation proceedings

67. On 7 July 2004 the applicant company filed a cassation appeal against the judgments of 26 May and of 29 June 2004 with the Federal Commercial Court of the Moscow Circuit ("the Circuit Court"). The applicant company's brief came to 77 pages and had 6 documents in annex. The arguments in the brief were largely similar to those raised by the applicant company on appeal, namely that the judgment was unlawful and unfounded, that the entities mentioned in the report ought to have taken part in the proceedings, that the trial court had had insufficient evidence to conclude that the applicant

company and other entities were interrelated, that the evidence used by the trial court was unlawful, that the trial proceedings had not been adversarial and that the principle of equality of arms had been breached. In addition, the company alleged that it had had insufficient time to study the evidence and had been unable to contest the evidence in the case, that the Ministry had unlawfully applied to a court before the applicant company had had an opportunity to comply voluntarily with the decision of 14 April 2004, that the entities mentioned in the report had in fact been eligible for the tax exemptions, that the rules governing tax exemption had been wrongly interpreted, that the Ministry's claims had been time-barred, that the company had had insufficient time for the preparation of the appeal, and that the case ought to have been examined by a court in Nefteyugansk.

68. A copy of the reasoned version of the appeal judgment of 29 June 2004 was attached to the brief.

69. It appears that on an unspecified date the Ministry also challenged the judgments of 26 May and 29 June 2004.

70. On 17 September 2004 the Circuit Court examined the cassation appeals and upheld in substance the judgments of 26 May and 29 June 2004.

71. In respect of the applicant company's allegations of unfairness in the appeal proceedings, the court noted that both defendant companies had had ample opportunities to avail themselves of their right to bring appeals within the statutory time-limit, as the appeal decision was not taken until 29 June 2004, which was more than thirty days after the date of delivery of the judgment of 26 May 2004. Furthermore, the court observed that the evidence presented by the Ministry and examined by the lower courts was lawful and admissible, and that it had been fully available to the defendant companies before the commencement of the trial hearings. The court also noted that on 14 May 2004 the City Court specifically ordered the Ministry to disclose all the evidence in the case, that this order had been complied with by the Ministry and that, despite the fact that the evidence was voluminous, the applicant company had had sufficient time to examine and challenge it repeatedly throughout the proceedings between May and July 2004.

72. As regards the applicant company's complaint that the Ministry had brought proceedings before the expiry of the time-limit for voluntary compliance with the decision of 14 April 2004, the court noted that the Ministry and lower courts had acted in compliance with Article 213 of the Code of Commercial Court Procedure, as there were irreconcilable differences between the parties and, throughout the proceedings, the applicant company had had insufficient funds to satisfy the Ministry's claims.

73. In respect of the applicant company's argument that the case should have been tried by a court in Nefteyugansk, the court noted that the City Court had had jurisdiction over the case under Article 54 of the Civil Code and decision no. 6/8 of the Plenary Session of the Supreme Court and Supreme Commercial Court of 1 July 1996.

74. On the merits of the case, the court noted that the lower courts had reached reasoned conclusions that the applicant company was the effective owner of all goods traded by the sham companies registered in low-tax areas, that the transactions of these entities were in fact those of the applicant company, that neither the applicant company nor the sham entities were eligible for the tax exemptions and that the applicant company had perceived the entirety of the resulting profits. The court upheld the lower courts' conclusion that, acting in bad faith, the applicant company had failed properly to declare its transactions for the year 2000 and to pay corresponding taxes, including VAT, profit tax, motorway users' tax, property tax, the tax for the maintenance of the housing stock and socio-cultural facilities and tax on the sale of fuel and lubricants.

75. The court noted some arithmetical mistakes in the appeal judgment of 29 June 2004, increasing the penalty by RUB 1,158,254.40 (approximately EUR 32,613) and reducing the default interest by RUB 22,939,931 (approximately EUR 645,917) accordingly.

(i) Constitutional review

76. On an unspecified date the applicant company lodged a complaint against the domestic courts' decisions in its case with the Constitutional Court. It specifically raised the question of the lower courts' refusal to apply the statutory time-limit set out in Article 113 of the Tax Code.

77. By decision of 18 January 2005 the Constitutional Court declared the complaint inadmissible for lack of jurisdiction. The court noted that the applicant company did not in fact challenge the constitutionality of Article 113 of the Code but rather insisted that this provision was constitutional and should be applied in its case. Therefore, the applicant company was not complaining about the breach of its rights by the above-mentioned provision and, accordingly, the court had no competence to examine the applicant company's claims.

(j) Supervisory review

78. Simultaneously to bringing the cassation appeal, on 7 July 2004 the applicant company also challenged the judgments of 26 May and 29 June 2004 by way of supervisory review before the Supreme Commercial Court of Russia.

79. On 31 December 2004 the applicant company's case was accepted for examination by the Supreme Commercial Court.

80. By a decision of 13 January 2005 the Supreme Commercial Court, sitting as a bench of three judges, decided to relinquish jurisdiction in favour of the Presidium of the Supreme Commercial Court. Addressing one of the applicant company's arguments, the court noted that the lower courts had decided that the three-year statutory time-bar was inapplicable in the case at issue since the applicant company had been acting in bad faith. It further

noted that such an interpretation of the rules governing the time-limits was not in line with the existing legislation and case-law and that therefore the issue should be resolved by the Presidium of the Supreme Commercial Court.

81. On 19 April 2005 the Presidium of the Supreme Commercial Court referred the above-mentioned issue to the Constitutional Court and adjourned the examination of the applicant company's supervisory review appeal pending a ruling by the Constitutional Court.

82. By a decision of 14 July 2005 the Constitutional Court decided that it was competent to examine the question of the compatibility of Article 113 of the Tax Code with the Constitution, having cited the application of an individual, one G. A. Polyakova, and the referral by the Supreme Commercial Court. At the same time, it noted specifically that it had no competence to decide individual cases and its ruling would only deal with the points of law *in abstracto*.

83. It appears that the legal issues raised by G. A. Polyakova and the applicant company were different. G. A. Polyakova was dissatisfied with the established court practice which required the tax authorities, rather than the courts, to hold a taxpayer liable for a tax offence within the three-year time-limit set out in Article 113 of the Code. On the facts of her individual case, the decision of the tax authorities was taken on time, whilst later the final decision by the courts was taken outside the specified time-limit. As regards the applicant company, it raised the same point which had been previously declared inadmissible by the Constitutional Court in its decision dated 18 January 2005, namely the refusal of the courts in its case to follow the established practice and to declare the claims of the authorities time-barred, as they related to the year 2000 and were set out in the decision to hold the applicant liable for a tax offence on 14 April 2004, that is, outside the three-year time-limit laid down by Article 113 of the Code.

84. As a result of its examination, the Constitutional Court upheld Article 113 of the Tax Code as compatible with the Constitution, having ruled that the legal provisions on the statutory time-limits ought to be applied in all cases without exception. The court made an abstract review of the provision in question and mentioned the "principles of justice", "legal equality" and "proportionality" in giving its own "constitutional interpretation" of Article 113. The court noted that the rule set out in Article 113 of the Code was too strict and failed to take into account various relevant circumstances and the actions of taxpayers, including those aimed at hindering tax control and delaying the proceedings. It further ruled that:

> "... the provisions of Article 113 of the Tax Code of the Russian Federation in their constitutional and legal sense and in the present legal context do not exclude [the possibility] that, where the taxpayer impedes tax supervision and the conduct of tax inspections, the court may excuse the tax authorities' failure to bring the proceedings in time ..."

> "... In their constitutional and legal sense in the context of the present legal regulation... [these provisions] mean that the running of the statutory time-bar in respect of a person prosecuted for tax offences stops on the date of the production of the tax audit report in which the supported facts of the tax offences revealed during the inspection are mentioned and in which there are reference to the relevant articles of the Tax Code or - in cases where there was no need to produce such a report - from the moment on which the respective decision of the tax authority, holding a taxpayer liable for a tax offence, was taken. ..."

85. Three out of the nineteen judges filed separate opinions in this case.

86. Judge V. G. Yaroslavtsev disagreed with the majority, having noted that the Constitutional Court acted *ultra vires* and openly breached the principle of lawfulness by creating an exception from the rule set out in Article 113 where there had previously been none.

87. Judge G. A. Gadzhiev concurred with the conclusions of the majority but would have preferred to quash, rather than uphold, Article 113 of the Tax Code as unconstitutional and breaching the principle of equality.

88. Judge A. L. Kononov dissented from the majority ruling, having considered that the Constitutional Court clearly had no competence to decide the matter and that indeed there had been no constitutional issue to resolve as, among other things, there had been no prior difficulties in application of Article 113 of the Tax Code and the contents of this provision had been quite clear. He also criticised the "inexplicable" way in which the Constitutional Court had first rejected the application by the applicant company and had then decided to examine the matter again. Judge Kononov further noted that the decision of the Constitutional Court was vague, unclear and generally questionable.

89. The case was then returned to the Presidium of the Supreme Commercial Court.

90. On 4 October 2005 the Presidium of the Supreme Commercial Court examined and dismissed the applicant company's appeal. In respect of the company's argument that the Ministry's claims were time-barred, the court noted that during the tax proceedings the company had been actively impeding the tax inspections. In view of this and given the Constitutional Court's ruling, the court concluded that since the Ministry's tax audit report in the applicant's case had been completed on 29 December 2003, that is, within the statutory three-year time-limit as interpreted in the Constitutional Court's decision of 14 July 2005, the case was not time-barred.

2. Enforcement measures relating to the 2000 Tax Assessment

91. Simultaneously with the determination of the case before the courts in respect of the applicant company's tax liability for the year 2000, the parties also took part in various enforcement proceedings.

(a) Attachment of the applicant's property

(i) The City Court's decision of 15 April 2004

92. On 15 April 2004 the City Court accepted for consideration the Ministry's action in respect of the year 2000 and attached certain of the applicant company's assets, excluding goods produced by the company and related cash transactions, as a security for the claims. The court also issued writs of execution in this respect (see paragraph 27). This decision was upheld by the Appeal Court on 2 July 2004.

(ii) Enforcement of attachment by the bailiffs

93. By a decision of 16 April 2004 the bailiffs instituted enforcement proceedings in connection with the attachment.

94. On the same day they executed the attachment order by informing the applicant company and the holder of its corporate register, ZAO 'M-Reestr', of the decision of 15 April 2004.

95. According to the Government, the applicant company impeded the execution of the writs issued by the court by hiding its corporate register from the bailiffs. In particular, they alleged that a few hours prior to the bailiffs' visit, the applicant company had cancelled its contracts with ZAO 'M-Reestr'. The register was then dispatched by ordinary post to a location in Russia so that, over the next weeks, it could not be physically found and the execution writs could not be enforced.

(iii) The company's offer of 22 April 2004

96. On 22 April 2004 the applicant company filed its first court request to have the attachment of the entirety of its assets replaced by the attachment of shares belonging to it in OAO Sibirskaya neftyanaya kompaniya ("the Sibneft company", a major Russian oil company which had attempted unsuccessfully to merge with the applicant company in 2003), which were allegedly worth three times as much as the then liability. The applicant company also alleged that the attachment order adversely affected its proper functioning and invited the authorities to opt for less intrusive measures, insisting on the lack of any risk of asset-stripping.

97. By a decision of 23 April 2004 the City Court examined and dismissed this request as unfounded. The court found no evidence that the interim measures affected any of the company's production activities.

98. On 17 May 2004 the applicant company appealed against the decision of 23 April 2004.

99. The outcome of court proceedings in respect of the applicant company's appeal of 17 May 2004 is unclear.

100. The Government provided the following background information in connection with the company's offer of shares in Sibneft. The applicant

company had attempted to merge with Sibneft in May-September 2003. As a result of the initial stages of the merger, the applicant company acquired 92% of Sibneft: 20% of these shares were bought for cash, whilst 57.5% were exchanged for 17.2% of the applicant company's newly issued shares and 14.5% were swapped for 8.8% of the applicant company's existing shares. In November 2003 it was announced publicly that, at the request of the former Sibneft owners, the parties had decided not to go ahead with the merger. In February 2004 the owners of Sibneft sued the applicant company in this connection, demanding cancellation of the operation whereby the applicant had issued 17.2% of shares. Among other things, on 14 February 2004 they obtained an attachment order in respect of the Sibneft shares remaining in the possession of the applicant company pending the proceedings. On 1 March 2004 the City Court decided to cancel the issue of 17.2% shares by the applicant company. The Government submitted that it was clear from the above-mentioned account that on 22 April 2004, the date on which the applicant company first made the offer of Sibneft shares, the owners of Sibneft already anticipated suing the applicant company again, this time demanding back the 57.5% of Sibneft shares swapped for the cancelled 17.2% of the applicant company's shares. At the same time, the fate of the remaining issues of Sibneft shares still in the possession of the applicant company was also uncertain.

(iv) The applicant company's request for an injunction against the attachment

101. On 23 April 2004 the City Court also examined the applicant company's request for an injunction order against the attachment and rejected it. The court noted that the attachment did not interfere with the company's day-to-day operations and it was a reasonable measure aimed at securing the Ministry's claims.

102. On 2 July 2004 the Appeal Court rejected the company's appeal and upheld the judgment.

103. It does not appear that the applicant company brought cassation proceedings in this respect.

(b) Enforcement of the Tax Ministry's decision of 14 April 2004

104. In the meantime, on 7 May 2004 the applicant company applied to the City Court with a separate action against the tax assessment of 14 April 2004, seeking its invalidation (see paragraph 34 and 35 above). The company also requested interim measures in this connection.

105. Following the applicant company's request for interim measures, on 19 May 2004 the City Court stayed the enforcement of the Tax Ministry's decision of 14 April 2004, having noted that the Ministry could have enforced the decision in the part relating to taxes and default interests even without

waiting for the outcome of the Ministry's claim (Article 46 of the Tax Code[2]). The court decided, however, that this might be detrimental to the applicant company and stayed the decision of 14 April 2004 accordingly.

106. On 27 May 2004 the applicant company made a public announcement that:

> "... it [was] under an injunction prohibiting it from selling any of its property, including the shares owned by the company. Until the injunction is lifted, the Company is unable to sell its assets in order to obtain liquid funds. Consequently, if the Tax Ministry's efforts continue, we are very likely to enter a state of bankruptcy before the end of 2004".

107. It appears that the City Court's decision of 19 May 2004 to stay the enforcement was appealed against by the Ministry. Having examined the Ministry's arguments at the hearing of 23 June 2004, the Appeal Court quashed the first-instance decision of 19 May 2004 as unlawful and rejected the applicant company's request for interim measures as unfounded.

108. It does not appear that the applicant company appealed against this decision before the Circuit Court.

(c) Enforcement of the judgments concerning the 2000 Tax Assessment

(i) First-instance judgment of 26 May 2004 and the appeal decision of 29 June 2004

109. As mentioned above (paragraphs 46-66), by a judgment of 26 May 2004 the City Court found in favour of the Tax Ministry, upholding the Tax Assessment of 14 April 2004. The Tax Assessment was upheld by the Appeal Court with minor reductions and became enforceable on 29 June 2004.

110. On 30 June 2004 the Appeal Court issued the writ of enforcement in this respect. The applicant company was to pay RUB 47,958,133,380 (approximately EUR 1,358,914,565) in reassessed taxes, RUB 32,190,430,314 (approximately EUR 912,129,842) in interest surcharges and RUB 19,185,272,697 (approximately EUR 543,623,045) in penalties.

(ii) Enforcement proceedings in respect of the writ of 30 June 2004

111. On 30 June 2004 the bailiffs instituted enforcement proceedings based on the above judgment and gave the applicant company five days to pay. The applicant company was informed that it would be liable to pay enforcement fees of 7%, totalling RUB 6,953,375,547 (approximately EUR 197,026,920), in the event of failure to honour the debt voluntarily. Upon the Ministry's application, the bailiffs issued sixteen orders freezing the

[2] Rectified on 17 January 2012 : the text was: "Article 46 of the Code of Commercial Court Procedure"

cash held by the applicant company in its Russian bank accounts. The orders did not concern cash added to the accounts after 30 June 2004.

(iii) The applicant company's challenge to the decision of 30 June 2004

112. On 7 July 2004 the applicant company challenged the bailiffs' decision of 30 June 2004.

113. It argued that the decision to open enforcement proceedings had been unlawful as it was in breach of the rules of bailiffs' territorial competence as the enforcement ought to have taken place in Nefteyugansk and not in Moscow, that the five-day term for voluntary compliance with the court decisions had been too short and that the cash-freezing orders had made such compliance impossible.

114. On 30 July 2004 the City Court examined and dismissed these claims as groundless. The court ruled that the bailiffs had acted lawfully and that the cash-freezing orders did not interfere with its ability or inability to honour its debts, as the applicant company had been free to dispose of any cash not in the frozen accounts and any cash added to those accounts after 30 June 2004.

115. It does not appear that the company brought appeal proceedings against this judgment.

(d) Seizure of 24 subsidiary companies and related proceedings

116. In the meantime, on 1 July 2004 the bailiffs decided to seize 24 subsidiary companies belonging to the applicant company.

117. The applicant appealed against the decision in court.

118. By a first-instance judgment of 17 September 2004 the appeal was dismissed as unfounded. The judgment was produced on 20 September 2004.

119. The applicant did not appeal against the judgment before the Appeal Court, though it did bring further appeal proceedings before the Circuit Court.

120. On 2 February 2005 the judgment was upheld by the Circuit Court.

(e) The applicant company's proposal of 5 July 2004 and related proceedings

121. In addition to the above attempts to stay the enforcement of the judgments concerning the 2000 Tax Assessment, the applicant company, by a letter dated 2 July and filed on 5 July 2004, suggested to the bailiffs for the second time that it repay its debts by using 34.5% of Sibneft stock allegedly worth over 4 billion United States dollars ("USD", or some EUR 3.3 billion), citing its vertically integrated structure as a possible reason for seeking to find the least intrusive solution as well as the need to honour its contractual debts.

122. The Government provided the following background information in connection with the applicant's second offer of Sibneft shares (see paragraph 121 above). At this point, the owners of Sibneft had already obtained a court judgment in their favour by the City Court on 1 March 2004, ordering the applicant company to return the 57.5% of Sibneft shares swapped for the cancelled 17.2% of the applicant company's shares and on

6 July 2004, that is, on the day after the applicant's second offer, they had filed court claims demanding the return of 14.5% of the shares previously exchanged for 8.8% of the applicant company's existing shares. In addition, by a decision of 6 July 2004 the owners of Sibneft had obtained an attachment order in respect of the Sibneft shares in question.

123. On 14 July 2004 the applicant company filed an action against the bailiffs on account of their alleged failure to respond to the company's offer of 5 July 2004.

124. On 17 August 2004 the City Court dismissed this action, having noted that the failure to respond was lawful and within the scope of the bailiffs' discretion. The court established that some of the steps undertaken by the applicant company during the unsuccessful merger with the Sibneft company had been contested in a different set of proceedings as unlawful. In addition, the applicant company's ownership of the Sibneft shares had been contested by third parties in two different sets of proceedings. On the basis of these findings, the court concluded that the bailiff had not breached the law by ignoring the company's offer.

125. It does not appear that the applicant company appealed against the judgment.

(f) Default notice of 5 July 2004

126. On 5 July 2004 the applicant company received a default notice from syndicated lenders, a group of international banks, who had previously loaned the company USD 1 billion (EUR 821,894,430). The lenders considered that a default had occurred as a result of the recent and well-publicised events in respect of the applicant company and their actual or potential impact on the applicant company's business and assets. The notice stated that as a result of the default notice the loans were due and payable on demand.

(g) The company's cassation appeal of 7 July 2004 and the motion to stay the enforcement

127. As set out above (paragraph 67), on 7 July 2004 the applicant company filed a cassation appeal against the court judgments on the 2000 Tax Assessment and at the same time it moved to stay the enforcement proceedings. It argued that its assets were highly valuable, but that it had insufficient cash to honour the debts immediately and that the attachment of assets made any voluntary settlement impossible. The applicant company also argued that enforcement of the court judgments in the case would irreparably damage its business, since a reversal of the enforcement would be impossible.

128. By a decision of 16 July 2004 the Appeal Court agreed to consider the cassation appeal and, having examined the motion to stay the enforcement, dismissed it as unsubstantiated and unfounded, as the circumstances referred to by the applicant company were irrelevant under the

domestic law. The court noted that it would be possible to reverse the enforcement, since the plaintiff was the Treasury.

129. This decision was upheld by the Circuit Court on 4 August 2004.

(h) 7% enforcement fee

130. By a decision of 9 July 2004 the bailiffs levied an enforcement fee of 7% in respect of the applicant company's failure to comply with the execution writs of 30 June 2004 (see paragraph 110 above). The applicant company was to pay RUB 6,848,291,175.45 (approximately EUR 190,481,640)

131. On 19 July 2004 the applicant company challenged this decision in court.

132. By a decision of 3 August 2004 the City Court examined the applicant company's action and quashed the decision of 9 July 2004 as disproportionate and unjustified. The court decided that the enforcement fee could only be levied if the respondent had acted in bad faith and found that the bailiffs had failed to examine this question. The court also noted that 7% was the highest possible rate and that the bailiffs' decision failed to explain why the fee could not be lower. Among other things, the court referred to section 3 of Constitutional Court Ruling no. 13-P of 30 July 2001.

133. Following an appeal by the Ministry, on 27 August 2004 the Appeal Court quashed the decision of 3 August 2004 as erroneous and held that the bailiffs' actions had been lawful and justified. The court noted that the applicant company had failed to demonstrate that it had taken any steps to meet the liabilities. It further noted that the cash in the applicant company's accounts was only frozen in certain specified amounts and that, above those amounts, the company was free to function as usual. As to the company's proposal to offer the Sibneft shares as payment, the court noted that this could not be accepted, because the applicant company's property rights in respect of these shares had been questioned by a third party in a parallel set of proceedings. In addition, the court noted that the applicant company had failed to use a remedy provided in Article 324 of the Commercial Procedure Code.

134. The Circuit Court upheld the appeal decision on 6 December 2004.

(i) Overall debt in respect of 2000

135. Overall, in respect of 2000, the applicant company was ordered to pay RUB 99,333,836,391 (approximately EUR 2,814,667,452)

(j) The applicant company's proposal of 13 July 2004 and related proceedings

136. On 13 July 2004 the applicant company again repeated its offer of 34.5% of Sibneft shares to the bailiffs. On the next day the offer was amended to include only 20% of Sibneft shares. The domestic courts at three

instances analysed this offer in detail in their decisions of 6, 18 August and 25 October 2004 (see paragraphs 139-146 below).

(k) Seizure of shares in OAO Yuganskneftegaz

(i) Decision of 14 July 2004

137. On 14 July 2004 the bailiffs seized the shares of OAO Yuganskneftegas, one of the applicant company's principal production subsidiaries. The decision referred to the applicant company's inability to meet its liabilities. The attachment did not affect the applicant company's ability to manage OAO Yuganskneftegaz, but rather prevented the company from selling or encumbering those shares.

(ii) The applicant company's challenge to the decision of 14 July 2004

138. The applicant company appealed against this decision in court. With reference to section 59 of the Enforcement Proceedings Act, it argued that the bailiffs ought firstly to claim assets which were not involved in the production process, secondly those goods and other values which were not related to the production process and, thirdly, immovable objects, raw material and other main assets relating to the production cycle. In addition, the applicant company referred to Ruling no. 4 of the Plenary Supreme Commercial Court "On certain questions arising out of seizure and enforcement actions in respect of corporate shares", dated 3 March 1999, which suggested, in respect of those companies which had been privatised by the State as parts of bigger holding groups through the transfer of controlling blocks of shares, that the production cycle of the respective production unit should be preserved as much as possible. The company further claimed that the above ruling was applicable to the case at issue, that OAO Yuganskneftegas was a major production unit and that the bailiffs had produced no evidence that the assets and goods and other values not involved in the production process were insufficient. In addition, it reiterated its offer of the shares in Sibneft.

(iii) First-instance proceedings

139. On 6 August 2004 the City Court examined and allowed the applicant company's challenge of this seizure.

140. At the hearing the Ministry and bailiffs referred to sections 9 (5) and 51 (1-4) of the Enforcement Proceedings Act and Government Decree no. 934 "On seizure of securities" of 12 August 1998. They argued that, under the applicable domestic law, the seizure should be made first in respect of the cash-flow and then, under section 46 (5) of the Enforcement Proceedings, it would be open to the bailiffs to assess and seize the assets depending on their liquidity. They countered the applicant company's

arguments by saying that the latter's references were invalid in that they related to the other stage of enforcement proceedings (the collection of debt and not the seizure as such). Furthermore, they argued that Ruling no. 4 of the Plenum of the Supreme Commercial Court was inapplicable since, in the case of Yuganskneftegas, the State had transferred only 38% of the shares and not a controlling block. With regard to the offer of Sibneft stock, the Ministry and bailiffs argued that the applicant company's rights in respect of these shares had been contested in separate sets of court proceedings and it was therefore risky to accept them as a payment. Lastly, they informed the court that the applicant company had recently hidden the shareholder registers of its three major subsidiaries, OAO Yuganskneftegas, OAO Samaraneftegas and OAO Tomskneft, which, in their view, demonstrated the risk of possible asset-stripping by the applicant company.

141. Having examined the parties' submissions, the court upheld the applicant company's arguments. It noted that the applicant company's references to the applicable domestic law were correct. With regard to the non-controlling block argument, the court noted that at the time of transfer of the shares, 25% of shares were privileged and non-voting. For the remaining 75% of the voting stock, the 38% transferred by the State constituted the controlling block. As regards the offer of shares in Sibneft, the court noted that the exact quantity of the contested shares was unclear and that the bailiffs should find out the exact figures and that they should consider the uncontested shares as a possible means of partial settlement. The court concluded that the decision of 14 July 2004 was unlawful and quashed it.

(iv) Appeal proceedings

142. On 9 August 2004 the Ministry challenged the decision of 6 August 2004 on appeal.

143. On 18 August 2004 the Appeal Court quashed the decision, finding that the first-instance court had erred both in law and fact. In particular, the court confirmed that it was up to the bailiffs to choose the most liquid assets and dispose of them with a view to honouring the applicant company's huge debt. It also noted that Ruling no. 4 of the Plenary Supreme Commercial Court was inapplicable to the case in issue, as the applicant company, in the years following its privatisation, had restructured its initial shareholding in OAO Yuganskneftegaz in 1999 in such a manner as to take those shares outside the scope of the exception provided by Ruling no. 4.

(v) Cassation proceedings

144. Following an appeal by the applicant company, on 25 October 2004 the Circuit Court upheld the decision of 18 August 2004.

145. The applicant company's attempts to bring supervisory review proceedings against this decision proved unsuccessful.

146. The respective complaint was dismissed by a decision of the Supreme Commercial Court dated 17 December 2004.

(l) Seizure of shares of OAO Tomskneft-VNK and OAO Samaraneftegaz

147. In addition to seizing the shares of OAO Yuganskneftegaz, on 14 July 2004 the bailiffs also seized the shares of OAO Tomskneft-VNK and OAO Samaraneftegas, the applicant company's two other principal production units.

148. The applicant company's complaint against the seizure of OAO Tomskneft-VNK proved unsuccessful.

149. The City Court dismissed its complaint as unfounded on 13 August 2004.

150. The applicant company did not contest that judgment before the Appeal Court.

151. On 5 November 2004 the Circuit Court dismissed the applicant company's cassation appeal in respect of the judgment of 13 August 2004. The court noted that the seizure was intended to protect the creditor's claims and that there was no indication that the seizure impeded the production cycle or otherwise disturbed the normal functioning of the company.

152. The company also complained unsuccessfully about the seizure of its shares in OAO Samaraneftegaz.

153. The City Court, acting as a first-instance court, dismissed the appeal on 2 September 2004.

154. The applicant company failed to appeal the judgment before the Appeal Court, although though it did pursue cassation proceedings.

155. On 18 January 2005 the Circuit Court upheld the judgment.

(m) The applicant company's request to the Ministry of Finance dated 16 July 2004

156. On 16 July 2004 the applicant company wrote a letter to the Ministry of Finance, applying for respite or payment in instalments in respect of the sums due. It appears that this letter remained unanswered. The Government submitted that the Ministry of Finance had not had any authority to respond to the request, as the issue of respite and payment in instalment lay within the competence of the courts.

157. On 12 August 2004 the City Court examined the applicant company's request to re-pay the 2000 Tax Assessment award in instalments and rejected it as unfounded. The court noted, among other things, that the tax debt had resulted from intentional tax evasion by the applicant company and that the conduct of the debtor in court and during the enforcement proceedings demonstrated that it did not intend to pay the debts voluntarily.

158. It does not appear that the applicant company brought any appeal proceedings in respect of this judgment.

(n) The applicant company's offer of 9 August 2004

159. On 9 August 2004 the applicant company offered the bailiffs the 20% stake in Sibneft and shares in fifteen other subsidiary companies as a settlement for its debts, requesting that the bailiffs respond within one day.

160. It appears that the bailiffs responded to the company's offer on 9 September 2004. It does not appear that the company brought any court proceedings in respect of that response.

(o) The Ministry's response of 22 September 2004

161. It appears that on 22 September 2004 the Ministry responded to four of the applicant company's letters about the settlement of the debt, rejecting the offers.

162. It does not appear that the company brought any separate court proceedings in this respect.

(p) The applicant company's announcement in respect of the shares in Sibneft

163. On 8 October 2004 the applicant company announced that it would comply with the City Court's judgment of 1 March 2004, which had cancelled the issue of additional shares in the applicant company, used for the purpose of acquiring Sibneft. The applicant company, acting in compliance with the court order, instructed the registrar to return its 57.5% stake in Sibneft to its former owners.

B. Proceedings in respect of the applicant company's tax liability for the year 2001

1. Tax Assessment 2001

(a) Proceedings before the Ministry

164. On 23 March 2004 the Tax Ministry commenced tax inspection in respect of the applicant company's activities in 2001. The inspection ended on 30 June 2004 and on 5 July 2004 the Ministry served the resultant report on the applicant company.

165. On the basis of the above-mentioned report, by a decision of 2 September 2004 the Ministry issued a tax assessment for the year 2001 ("the 2001 Tax Assessment"), finding the company liable for having used essentially the same tax arrangement as in the previous year. The Tax Assessment 2001 relied on a similarly wide range of evidence as the Tax Assessment 2000, including the documentary evidence and detailed statements of those involved in the nominal ownership and running of the trading companies. This time the applicant company had to pay RUB 50,759,436,900 (approximately EUR 1,424,746,313) in tax arrears,

RUB 28,520,204,254 (approximately EUR 800,522,195) in default interest and RUB 40,607,549,520 in penalties (approximately EUR 1,139,797,051). Since the applicant company had recently been found guilty of a similar offence, the penalty was doubled.

(b) The applicant company's request for a court injunction

166. On 14 September 2004 the applicant company lodged an appeal against the decision of 2 September 2004 and requested an injunction against the immediate enforcement of this decision.

167. On 5 October 2004 the City Court turned down the request for an injunction and on 13 October 2004 it issued execution writs in respect of the Ministry's decision of 2 September 2004. The court referred to Information Letter no. 83 of the Supreme Commercial Court of 13 August 2004, which recommended that requests for interim measures in such situations be granted only if an applicant could demonstrate some security for a creditor's future claims. The court noted that, in the present case, the applicant company clearly had insufficient cash to satisfy the creditor's claims, and had failed to produce any security, and dismissed the claims accordingly.

168. The judgment of 5 October 2004 was upheld by the Appeal Court on 3 December 2004 and by the Circuit Court on 29 March 2005.

2. Enforcement measures relating to the 2001 Tax Assessment

(a) Enforcement of additional taxes and interest surcharges

169. As the 2001 Tax Assessment was similar to the 2000 Tax Assessment, the Ministry decided to enforce it directly in the part relating to additional taxes and interest surcharges, without taking the matter to the courts. The applicant company was to pay the amounts due by 4 September 2004.

170. On 9 September 2004 the bailiffs instituted enforcement proceedings in connection with the decision of 2 September 2004. The company was to pay RUB 50,759,436,900 (approximately EUR 1,424,746,313) in tax arrears and RUB 28,520,204,254 (approximately EUR 800,522,195) in default interest.

171. It appears that the 2001 Tax Assessment, in the part relating to additional taxes and interest surcharges, was upheld by the City Court on 11 October 2004. The judgment of 11 October 2004 was upheld on appeal on 16 February 2005. The Circuit Court upheld the decisions of the lower courts on 9 December 2005.

172. The applicant company's request for an injunction pending those proceedings was unsuccessful. The City Court dismissed it in its judgment of 5 October 2004. The refusal was upheld by the Appeal Court on 3 December 2004 and by the Circuit Court on 29 March 2005.

(b) Enforcement of penalties

173. On 3 September 2004 the Ministry applied to the City Court to recover the penalties arising from the 2001 Tax Assessment. .

174. It appears that on 11 October 2004 the action was examined and granted by the City Court. The judgment in the case was produced on 15 October 2004.

175. According to the applicant company, its appeal against the judgment of 15[3] October 2004 was dismissed by the Appeal Court on 18 November 2004. It appears that the Circuit Court upheld these two decisions on 15 November 2005.

176. On 19 November 2004 the bailiffs instituted enforcement proceedings in respect of the Tax Assessment 2001 in the part relating to penalties. The company was to pay RUB 39,113,140,826 in penalties (approximately EUR 1,097,851,399)[4].

(c) 7% enforcement fee in respect of additional taxes and interest surcharges

177. On 20 September 2004 the bailiffs decided to impose a 7% enforcement fee in respect of the applicant company's failure to abide by the 2001 Tax Assessment in the part relating to taxes and interest surcharges. The applicant company was to pay RUB 5,549,574,880.78 (approximately EUR 155,693,193).

178. The resolution was served on the applicant company on 1 October 2004.

179. On 29 October 2004 the City Court examined and dismissed the challenge to the decision of 20 September 2004 as groundless.

180. It does appear that the company pursued appeal proceedings.

181. On 1 December 2004 the company appealed in cassation against the judgment of 29 October 2004.

182. The appeal was dismissed by the Circuit Court on 3 March 2005.

(d) 7% enforcement fee in respect of penalties

183. On 9 December 2004 the bailiff decided to impose a 7% enforcement fee in respect the applicant company's failure to abide by the 2001 Tax Assessment in the part relating to penalties. The company was to pay a 7% enforcement fee of RUB 7,102,488,295 or approximately EUR 190,077,377.

184. On 23 December 2004 the company challenged this decision in court.

185. On 3 February 2005 the City Court dismissed the action.

186. The applicant company failed to appeal the judgment of 3 February 2005.

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[3] Rectified on 17 January 2012: the text was: "the judgment of 11 October 2004"

[4] Rectified on 17 January 2012: the text was: "RUB 40,607,549,520 in penalties (approximately EUR 1,139,797,051)"

187. The Circuit Court upheld the judgment of 3 February 2005 on 16 June 2005.

(e) Overall debt in respect of 2001

188. Overall, in respect of 2001 the applicant company was ordered to pay RUB 132,539,253,849.78 (approximately EUR 3,710,836,129).

C. Proceedings in respect of the applicant company's tax liability for the year 2002

1. Tax Assessment 2002

189. On 29 October 2004 the Ministry produced an audit report in respect of the applicant company's activities for the year 2002. The report was received by the company on 1 November 2004.

190. On 16 November 2004 the Ministry took a decision to levy further tax liabilities, this time in respect of the year 2002 ("the 2002 Tax Assessment"). The applicant company was to pay RUB 90,286,552,485 (approximately EUR 2,425,825,387) in taxes, RUB 31,485,110,355.58 (approximately EUR 845,944,140) in default interest and RUB 72,040,907,796 (approximately EUR 1,935,600,133) in penalties.

191. The decision established the use of the same tax-evasion scheme (in respect of profit tax, VAT, corporate property tax and motorway users' tax) as in the decisions concerning the years 2000 and 2001. It mentioned that the company had carried out its activities through OOO Ratmir, OOO Alta-Treid, ZAO Yukos-M, OOO Yu-Mordoviya, OOO Ratibor, OOO Petroleum treyding, OOO Evoyl, OOO Fargoyl, most of which had also been used by the applicant company in previous years. The entities in question, acting in breach of Article 575 of the Civil Code, which prohibits grants and gifts between independently functioning commercial entities, had transferred the entirety of their profits unilaterally to a fund owned and controlled by the applicant company. The decision mentioned that the transfers had been wrongly reflected in the applicant company's financial accounting and that the company had failed to explain the origin of these funds and had failed to take these sums into account for tax purposes. Accordingly, the applicant company had failed to pay taxes in respect of these amounts.

192. The decision referred to several other mistakes in the applicant company's tax declarations. In particular, the tax in respect of the company's securities transactions was wrongly calculated, there were many general mistakes in the company's financial accounting, and there were some mistakes in the company's request for reimbursement of the VAT on export operations (e.g. on one occasion the company failed to submit the required sales contract; it also mentioned one contract but received the money on the

basis of a different contract; on some occasions the company failed to submit documents proving customs clearance, indicated wrongly calculated sums, and made multiple mistakes in VAT export documents). There were further multiple mistakes in tax deductions in respect of internal VAT.

193. The decision also established that the applicant company had used sham entities to lower its group taxes, that the entities and the company's subsidiaries had entered into transactions with reduced prices, that on some occasions the company had declared the extracted oil as "hydrocarbon liquid" in order to lower the applicable price even further, that there were no cash transactions between the entities and subsidiaries and that the company's own promissory notes and mutual offsetting had been used instead and that the whole set-up, which had no economic purpose other than tax evasion, had resulted in massive tax evasion by the applicant company. The decision also noted that use of tax concessions in the Republic of Mordoviya and the Evenk Autonomous District by the sham entities had been unlawful, because they had failed to qualify for the exemptions and also because they had been sham companies. The decision was detailed in respect of the composition and all the activities of the sham entities: the Ministry analysed the entirety of their activities month by month.

194. The applicant company had until 17 November 2004 to meet the debts voluntarily.

2. Enforcement measures relating to the 2002 Tax Assessment

(a) Enforcement of additional taxes, interest surcharges and penalties

195. By a decision of 18 November 2004 bailiffs proceeded to enforcement of the decision of 16 November 2004 in so far as it related to additional taxes and interest surcharges.

196. The City Court joined the proceedings by which the applicant company tried to contest the decision of 16 November 2004 and on 23 December 2004 it examined and, in the most part, dismissed the applicant company's appeals against the decision of 16 November 2004. The court declared the Ministry's conclusions partly unfounded and reduced the company's tax liability by RUB 325,628,742 (approximately EUR 8,752,543), its default interest payments by RUB 98,515,758 (approximately EUR 2,647,995) and the penalty by RUB 851,419,688 (approximately EUR 22,885,227). The court also ordered the applicant to pay the penalty in question.

197. This decision was upheld by the Appeal Court on 5 March 2005 and the Circuit Court on 30 June 2005.

198. On 28 December 2004 the applicant company also appealed against the Ministry's decision in respect of the year 2002, in so far as it had ordered that the tax debts and default interest payments be collected directly.

199. It appears that on 7 February 2005 the City Court examined and dismissed the claim as unfounded. The judgment was upheld on appeal on 4 April 2005. The Circuit Court upheld the decisions of the lower courts on 15 June 2005.

(b) 7% enforcement fee in respect of additional taxes and interest surcharges

200. On 9 December 2004 the bailiffs decided to impose a 7% enforcement fee in respect of the applicant company's failure to comply voluntarily with the 2002 Tax Assessment in the part relating to additional taxes and surcharge interests.

201. On 23 December 2004 the company appealed against this decision in court, initially claiming that the decision had been unlawful and asking to reduce the fee to 1%. The company then withdrew its claim in the part relating to the reduction of the fee.

202. On 10 February 2005 the City Court judgment dismissed the appeal.

203. It does not appear that the company brought any proceedings before the Appeal Court in respect of the judgment.

204. The applicant company's cassation appeal was examined and dismissed by the Circuit Court on 16 June 2005.

(c) Overall debt in respect of 2002

205. Overall in respect of the year 2002 (excluding the 7% enforcement fee), the applicant company was ordered to pay RUB 192,537,006,448.58 (approximately EUR 4,344,549,434).

(d) Written information report communicated by ZAO PricewaterhouseCoopers Audit to the applicant company's management in respect of the year 2002

206. In their observations of 15 April 2005 the Government submitted a copy of a report communicated to the applicant company's management by its auditor ZAO PricewaterhouseCoopers Audit. The applicant company did not comment on the contents of the report.

207. In contrast to "ordinary" audit reports, which were made public, the internal information report was produced exclusively for the applicant company's management.

208. The report noted specifically that the applicant company's "Fund for Financial Support of the Production Development of OAO Neftyanaya Kompaniya YUKOS" was in breach of the domestic law in that the relevant legislation disallowed unilateral transfers and gifts between commercial entities. It also noted that the applicant company's accounting policy in respect of the operations involving promissory notes had been incompatible with the legislation in force and provided a distorted view of the company's activities.

209. In addition, on 15 June 2007 the applicant company's auditor, ZAO PricewaterhouseCoopers Audit, disavowed its audit certifications in respect of the applicant company's financial statements for the years 1995-2004 on account of the applicant company's deliberate attempts to conceal its tax-evasion scheme, as well as its failure to disclose all relevant documents during the respective inspections conducted by the company's auditors at the time.

D. Proceedings in respect of the applicant company's tax liability for the year 2003

1. Tax Assessment 2003

210. On 28 October 2004 the Tax Ministry commenced a tax inspection in respect of the year 2003, which resulted in an audit report that was dated 19 November 2004 and served on the applicant company on the same date.

211. On the basis of the report, by a decision of 6 December 2004 the Ministry levied tax liabilities for the year 2003 ("the 2003 Tax Assessment"), consisting of RUB 86,228,187,852 (approximately EUR 2,327,114,103) in taxes, RUB 15,235,930,657.66 (approximately EUR 411,185,136) in default interest and RUB 68,939,326,976.40 (approximately EUR 1,860,524,778) in penalties.

212. The decision established that the company was guilty of having evaded taxes (in particular, VAT, profit tax and advertising tax) by using the same arrangement as in previous years. The decision mentioned the following entities registered either in the Republic of Mordoviya or the Evenk Autonomous District: OOO Yu-Mordoviya, ZAO Yukos-M, OOO Alta-Treyd, OOO Ratmir, OOO Energotreyd, OOO Makro-Treyd, OOO Fargoyl, and OOO Evoyl. It was alleged that the entities were sham and that they had made unilateral transfers to the applicant company, in breach of Article 575 of the Civil Code, that the applicant company had failed to reflect the transferred amounts as its profits, to account for them and to pay taxes in this connection and that the company had used lowered prices to avoid the payment of taxes. The decision contained a detailed contract-by-contract analysis of the sham entities' transactions.

213. The decision also mentioned that some of the applicant company's expenses were unjustifiably deducted from the company's taxable income, that the company failed to account for some of its operations with promissory notes, that there were some mistakes in calculation of the VAT owed by the company and that the company had evaded payment of advertising tax in Moscow.

214. The applicant company had one day to comply with the decision, that is, until 7 December 2004.

2. Enforcement measures relating to the 2003 Tax Assessment

(a) Enforcement of additional taxes, interest surcharges and penalties

215. On 9 December 2004 the bailiffs proceeded to enforcement of the decision of 6 December 2004 in so far as it related to taxes and interest surcharges.

216. It appears that the City Court joined the proceedings by which the applicant company tried to contest the decision of 9 December 2004 and on 28 April 2005 it examined the company's challenge. In respect of the company's request to recalculate automatically the export VAT on operations conducted by the sham entities in the course of these proceedings, the court noted the request was unsubstantiated and also lodged out of time. In particular, the company had failed to submit a proper claim with monthly calculations and evidence that the goods in question had indeed been exported. The court also addressed the applicant company's argument that Article 75 (3) of the Tax Code prevented the authorities from levying the interest surcharges. It noted that the provision in question only applied to cases in which the sole reason for the taxpayer's inability to pay tax debts was the seizure of its assets and cash funds. On the facts, the applicant company was unable to pay because it had insufficient funds and not because its assets were frozen. The court concluded that the applicant company's argument was unfounded. The court also reduced the amount of additional taxes to be paid to RUB 86,221,835,476.37 (EUR 2,399,884,085) and the amount of fines to RUB 68,918,264,491 (EUR 1,918,259,397). The amount of interest surcharges was reduced accordingly. The exact figure of the interest surcharges to be paid by the applicant is unclear.

217. The judgment was upheld on appeal on 16 August 2005.

218. The applicant company appealed on cassation.

219. On 5 December 2005 the Circuit Court upheld the decisions of the lower courts.

220. The bailiffs instituted enforcement proceedings in respect of the payment of fines on 4 October 2005.

(b) 7% enforcement fee

221. On 17 March 2006 the bailiffs decided to impose a 7% enforcement fee in respect of the applicant company's failure to comply voluntarily with the 2003 Tax Assessment. The applicant company was to pay RUB 7,102,488,296 (EUR 211,872,906) in respect of the unpaid reassessed taxes and interest surcharges and RUB 4,824,278,304 (EUR 143,912,080) in respect of the unpaid fines.

(c) Overall debt in respect of the year 2003

222. Overall, in respect of 2003 (excluding the 7% enforcement fee and the interest surcharges, the exact amount of which is unclear) the applicant company was ordered to pay RUB 155,140,099,967.37 (approximately EUR 4,318,143,482).

E. Forced auctioning of OAO Yuganskneftegaz

223. On 20 July 2004 the Ministry of Justice announced the forthcoming evaluation and sale of OAO Yuganskneftegaz as a part of its ongoing enforcement procedures.

224. On 22 July 2004 the applicant company announced that:

> "...the company management [is] currently making every effort to raise additional funds in order to repay, as soon as possible, the tax liability and to finance current operations. However, should those efforts prove unsuccessful and Yuganskneftegaz [be] sold, in the present circumstances, the management of the Company would be compelled to announce the bankruptcy of Russia's largest oil company".

1. Valuation report of 17 September 2004

225. On 17 September 2004 the valuation commissioned by the bailiffs and the Ministry of Justice from Dresdner Kleinwort Wasserstein, the investment branch of Dresdner Bank AG (working in Russia as ZAO Dresdner bank), for the purposes of the enforcement proceedings, estimated that 100% of shares in OAO Yuganskneftegas were worth between USD 15.7 and 18.3 billion (between EUR 15.2 and 17.7 billion), excluding the pending and probable tax liabilities of this entity.

226. The report evaluated 100% of the price of OAO Yuganskneftegaz as a separate entity and, having deduced its corresponding obligations, calculated the cost of its shares, on the basis of which it would be possible to calculate the price of one share in OAO Yuganskneftegaz.

227. It was specifically mentioned in the report that the valuation was not an opinion concerning the attainable price in the event of the sale of OAO Yuganskneftegaz or any kind of recommendation concerning the starting bid of the auction in the event of the sale of Yuganskneftegaz by the Ministry of Justice or any other State institution, or any recommendation concerning particular actions to be undertaken by the Ministry of Justice with a view to levying the judicially determined or estimated amount of the applicant company's tax debt.

228. Among the basic risks affecting the price of OAO Yuganskneftegaz, the report mentioned the tax claims, the validity of oil extraction licences, future oil prices, export quotas etc. The report also mentioned that the price of OAO Yuganskneftegaz as a part of the applicant company could be substantially different from the price of OAO Yuganskneftegaz as a separate

entity. The report also mentioned various valuations of OAO Yuganskneftegaz made by third parties, including investment institutions and banks, and ranging from USD 9 to 22 billion (between EUR 7.4 to 18.1 billion). It also mentioned that, because of the size of OAO Yuganskneftegaz, not many buyers would be financially capable of acquiring it.

229. The valuation (between USD 15.7 and 18.3 billion or EUR 15.2 and 17.7 billion) did not take account of already pending and probable tax claims against OAO Yuganskneftegaz. If and when lodged, these claims would "substantially influence the assessment" of the equity of OAO Yuganskneftegaz. The claims already announced (as on that date) were USD 951.3 million.

230. In carrying out the valuation, the report used the following three methods: the method of discounted cash flows, a method based on the analysis of comparable transactions, and a method based on the analysis of comparable publicly-held companies.

231. The report also specifically noted that:

> "...the decision concerning the starting bid of the auction is a tactical one and should strike a balance between the desire to reach the highest price on the one hand, and the need to attract the maximum number of potential buyers on the other. Because of this, the starting bid is most likely to be different from the assessment of the price."

2. Service of the valuation report on the applicant company on 13 October 2004

232. A copy of the valuation report was served on the applicant company on 13 October 2004.

233. It does not appear that the applicant company contested the report's valuations report before the courts.

234. On 21 October 2004 the bailiffs confirmed to the Ministry that they had collected 79,584,690,127 RUB (approximately EUR 2,183,447,331).

3. The applicant company's reply of 4 November 2004

235. On 4 November 2004 the applicant company responded to the valuation report. It disagreed with the decision to evaluate and sell OAO Yuganskneftegaz, and would have preferred to sell its other assets first. The applicant company informed the bailiffs that it had already honoured a major part of the debt (apparently referring to its tax liability for the year 2000 only) and that the remaining sum was USD 2.5 billion (around EUR 2 billion). The company claimed that it would be more reasonable to lift the seizure and let it dispose of its minor assets in order to honour the remaining debt.

236. As regards OAO Yuganskneftegas, the company referred to independent valuations by JP Morgan PLC, valuing the subsidiary at "no less

than USD 14 billion (some EUR 11 billion)" and "between USD 16.1 billion (EUR 12.6 billion) and USD 22.1 billion (EUR 17.378 billion), including tax liabilities" respectively.

237. The letter mentioned that the Ministry had brought tax claims against OAO Yuganskneftegaz totalling USD 2.903 billion.

4. The bailiffs' decision of 18 November 2004

238. On 18 November 2004 the bailiffs noted that the applicant company's debt to the Ministry on that date was RUB 204,902,386,620 (approximately EUR 5,506,781,584 or USD 7,147,250,717). Having referred to sections 4, 46 (6), 54 (2) and 88 of the Enforcement Proceedings Act, the bailiffs decided to sell 76.79 % of the shares in OAO Yuganskneftegas at an auction which would take place on 19 December 2004. The published minimum bidding price for 76.79 % of the shares in OAO Yuganskneftegas was RUB 246,753,447,303.18 (approximately USD 8.65 billion or EUR 6.63 billion).

239. The sale was entrusted to the Russian Fund of Federal Property ("the Property Fund"), a specialised State Institution in charge of organising sales of federal property and the property of those who had debts towards the State.

240. On the same date, the Property Fund issued a regulation setting out the parameters and rules that would govern the auction, including the number of shares to be sold (43 ordinary shares representing 76.79% of the capital of OAO Yuganskneftegaz), the starting price (RUB 248.6 billion or some USD 8.85 billion), the date and place of the auction (19 December 2004), the eligibility requirements for bidders (the auction was open to all perspective bidders, including foreign individuals and legal entities), which included a cash deposit of RUB 49.4 billion (USD 1.7 billion, or 20% of the starting price), to be paid no later than the day before the auction.

5. Court action against the decision of 18 November 2004

241. The decision of 18 November 2004 was challenged in court on 26 November 2004.

242. It appears that on 3 December 2004 the City Court dismissed the appeal against the decision of 18 November 2004.

243. On 21 January and 3 May 2005 that judgment was upheld on appeal and in cassation respectively.

244. The applicant company argued that the valuation report had failed to give a market valuation of the asset and that the decision of 18 November 2004 failed to mention a specific price for OAO Yuganskneftegaz. In response, the courts noted that 43 ordinary and 13 privileged shares in OAO Yuganskneftegaz had been seized by the bailiffs in satisfaction of the applicant company's liability, that the shares had been valued by ZAO Dresdner Bank and that the applicant company had been informed of all

of the bailiffs' actions in the course of the enforcement proceedings. They also noted that the seizure of shares in OAO Yuganskneftegaz had previously been declared lawful, that the applicant company had been properly notified of all of the steps taken by the bailiffs in the course of the enforcement proceedings and could bring court proceedings against them, that the valuation by ZAO Dresdner Bank had not been contested by the applicant in accordance with the special procedure provided for by the legislation in force, and that the bailiffs had properly indicated the amount of the applicant company's debt and requested the Fund to sell the amount of shares necessary to satisfy the debt.

6. Announcement about the sale of OAO Yuganskneftegaz

245. In the meantime, on 19 November 2004, the Russian Gazette, an official Government newspaper, published an announcement about the sale of 76.79% of shares in OAO Yuganskneftegaz at a public auction organised by the Property Fund. The only two conditions for participating in the auction were to file an application between 19 November and 18 December 2004 and to make a deposit payment.

246. On 10 December 2004 OOO Gazpromneft, ZAO Intercom and OAO First Venture Company filed applications with the Federal Antimonopoly Service and thus were expected to bid at the auction.

247. The media reported that OAO Gazprom, a parent company of OOO Gazpromneft, had begun negotiating a financing arrangement with a consortium of international banks to finance its bid at the auction. It was also reported that a number of non-Russian companies, such as ENI, Chevron Texaco, China National Petroleum Corporation and E.ON, had expressed interest in participating in the auction.

248. On 17 December 2004 the bailiffs noted that the applicant company's consolidated debt on that date, regard being had also to the 2001 Tax Assessment, was RUB 344,222,156,424.22 (EUR 9,210,844,560.93, or USD 12,365,545,256.86).

7. The applicant company's application for bankruptcy in the United States of America and its request for injunctive relief

(a) Filing of bankruptcy petition and request for injunctive relief

249. On 14 December 2004 the applicant company filed a voluntary petition under Chapter 11 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the Southern District of Texas, Houston Division ("the U.S. Bankruptcy Court").

250. Simultaneously, the applicant company filed a request for injunctive relief, pursuant to section 105 of the U.S. Bankruptcy Code in order, among other things, to enforce the automatic stay set out in

section 362 (a) of the Bankruptcy Code by enjoining certain parties from participating in the Yuganskneftegaz Auction. The request was directed specifically against "... defendants the Russian Federation, OOO Gazpromneft, ZAO Intercom, OAO First Venture Company, ABN Amro, BNP Paribas, Calyon, Deutsche Bank, JP Morgan and Dresdner Kleinwort Wasserstein ...".

(b) Scope of automatic stay

251. Under U.S. law, an automatic stay went into immediate effect when the applicant company filed for bankruptcy. The automatic stay protected the company's assets by preventing the creditors from collecting claims that arose prior to the bankruptcy filing or from taking "possession" or "control" of the applicant company's property covered under the filing.

(c) Temporary restraining order of 16 December 2004

252. On 16 December 2004, having examined the applicant company's request, the U.S. Bankruptcy Court issued a temporary restraining order barring certain specific entities from taking any actions with respect to the shares in OAO Yuganskneftegaz, including participation in the auction. Among other things, Judge Letitia Z. Clark stated the following:

> "... The court is mindful of the need for deference to the judicial determination of another jurisdiction. This is ... of exceptional importance when it involves that of agencies of another sovereign state. However, in the instant case, the [applicant company] has made a showing that it needs a short additional time to hold its shareholder meeting scheduled for December 20, 2004 and may elect to file for bankruptcy under Russian law in order to proceed with a more orderly adjustment of its assets and debts in accordance with Russian law or to continue to seek international arbitration ...".

253. The entities mentioned in the order were (a) the three companies registered to bid at the Auction, including OOO Gazpromneft, ZAO Intercom and OAO First Venture Company, (b) six western financial institutions that had announced their intention to fund OOO Gazpromneft's bid at the auction (ABN Amro, BNP Paribas, Calyon, Deutsche Bank, JP Morgan and Dresdner Kleinwort Wasserstein) and (c) those persons in active concert or participation with them.

(d) Outcome of the bankruptcy proceedings in the U.S.

254. On 24 February 2005 the U.S. Bankruptcy Court dismissed the applicant company's petition for bankruptcy with reference to section 1112 (b) of U.S. Bankruptcy Code which gave the court discretion to dismiss a case "in the best interest of the creditors and the estate".

255. The court noted that most of the applicant company's assets were oil and gas within Russia, so that the court's ability to carry out a re-organisation without the cooperation of the Russian government was

extremely limited, that the applicant company sought to substitute U.S. law in place of Russian, European Convention and/or international law, that the applicant company had commenced proceedings in other *fora*, including the European Court of Human Rights, and the court did not feel that it was uniquely qualified or more able that these other *fora* to consider the issues presented. Lastly, the court noted that the vast majority of the business and financial activities of the applicant company continued to occur in Russia and that the applicant company was one of the largest producers of petroleum products in Russia. The court held that "the sheer size of [the applicant company] and its impact on the entirety of the Russian economy weighs heavily in favour of allowing resolution in a forum in which participation of the Russian government is assured".

8. Auction of 19 December 2004

256. On 19 December 2004 the Property Fund auctioned 76.79% of the shares in OAO Yuganskneftegaz. It appears that media reporters were able to attend the auction.

257. There were two participants in the auction, OOO Baykalfinansgrup and OOO Gazpromneft. OOO Baykalfinansgrup, the only bidder in the auction, made two bids, first of USD 8.65 billion and then of RUB 260,753,447,303.18 (USD 9.4 billion or EUR 7.05 billion). It appears that whilst taking part in the auction OOO Gazpromneft was prevented from bidding by the injunction of 16 December 2004 (see paragraph 253 above).

9. The decisions and reports concerning the outcome of the auction

258. On 21 December 2004 the Ministry of Justice issued a report accepting that the Property Fund had properly carried out the services due under the contract of 18 November 2004.

259. On 21 December 2004 the Property Fund publicly reported the sale of the shares in OAO Yuganskneftegaz.

260. On 31 December 2004 the bailiffs issued a resolution confirming the results of the auction. The resolution stated that OOO Baykalfinansgrup had won the auction for 43 shares in OAO Yuganskneftegaz (76.79% of its stock) for RUB 260,753,447,303.18 (approximately EUR 6,896,341,940 or USD 9,396,960,842). By the time that resolution was issued, the money had already been transferred to the bailiffs.

10. Takeover of OOO Baykalfinansgrup by OAO Rosneft

261. According to press reports of 31 December 2004, OAO Rosneft, a State-owned oil company, acquired OOO Baykalfinansgrup and thus took control of OAO Yuganskneftegas.

262. In its consolidated financial statements 2003-2005, dated 15 May 2005,OAO Rosneft declared:

"... In late December 2004 [OAO Rosneft] acquired a 100% interest in [OOO Baykalfinansgrup], which a few days earlier had won an auction for the sale of a 76.79% interest in [OAO Yuganskneftegaz], which represents 100% of the common shares of [OAO Yuganskneftegaz]. ..."

11. Court proceedings in connection with the auction

263. It appears that on 26 May 2005 the applicant company filed an action in the City Court against the Property Fund, OOO Baykalfinansgrup, OAO Rosneft, OOO Gazpromneft, OAO Gazprom and the Ministry of Justice, seeking to annul the auctioning of 43 shares in OAO Yuganskneftegas and the deed of sale. It also claimed damages in excess of RUB 324 billion.

264. The action was examined and dismissed by the City Court on 28 February 2007. The court decided that both the Ministry of Justice and the Property Fund[5] had acted within their statutory powers, that the auction procedure had been fully complied with and that the applicant company's allegation about the auction participants acting in concert had been unsupported by any evidence.

265. The judgment was upheld by the Appeal Court on 30 May and by the Circuit Court on 12 October 2007.

266. On 27 January 2005 the applicant company also initiated parallel proceedings against OAO Rosneft, OOO Baykalfinansgrup, Deutsche Bank AG, Deutsche Bank AG London, Deutsche Bank Luxembourg S.A., Deutsche Bank Trust Company Americas and the Russian Federation before the U.S. Bankruptcy Court for violation of the automatic stay.

267. The applicant company voluntarily withdrew the entire proceedings on 28 March 2005, after its bankruptcy petition was dismissed by the U.S. Bankruptcy Court.

F. Bankruptcy proceedings

268. It does not appear that any enforcement measures took place in respect of the applicant company after the auctioning of OAO Yuganskneftegaz until September 2005.

269. On 8 September 2005 a consortium of foreign banks represented by the French bank Société Générale ("the banks") filed an application with the City Court for recognition and enforcement of an English High Court judgment ordering the applicant company to re-pay the contractual debt of USD 482 million (around EUR 385 million), resulting from the applicant company's default under a USD 1 billion loan agreement dated 24 September 2003.

[5] Rectified on 17 January 2012: "Fund" has been added.

270. On 22 September 2005, at the banks' request, the bailiffs again attached the applicant company's property.

271. In October 2005 the applicant company challenged this order.

272. On 30 November 2005 the City Court dismissed the appeal as groundless.

273. The first-instance judgment was upheld by the Appeal Court and by the Circuit Court on 27 February and 12 May 2006 respectively.

274. In the meantime, on 28 September 2005, the City Court allowed recognition and enforcement of the English High Court judgment.

275. On 5 December 2005 the Circuit Court granted the applicant company's cassation appeal and quashed the judgment of 28 September 2005. It remitted the case for a fresh hearing.

276. On 21 December 2005, having re-examined the case, the City Court allowed the banks' claims.

277. On 25 January 2006 the applicant company appealed against the judgment of 21 December 2005.

278. On 2 March 2006 the Circuit Court dismissed the appeal.

279. It appears that on 13 December 2005 the banks reached an agreement with the Rosneft company to sell to the latter the applicant company's debt to the banks.

280. On 6 March 2006 the banks lodged a petition with the City Court to declare the applicant company bankrupt.

281. On 9 March 2006 bankruptcy proceedings were initiated against the applicant company upon the banks' petition. It appears that the Ministry decided to join the proceedings as one of the bankruptcy creditors in respect of remaining tax debts of the 2000-2003 Tax Assessments still owed by the applicant company.

282. On 14 March 2006 the banks notified the City Court about the decision to sell the debts owed by the applicant company to Rosneft.

283. On 29 March 2006 the City Court substituted Rosneft in the place of the banks as a bankruptcy creditor. By the same decision the court imposed a supervision order on the applicant company and appointed Mr Eduard Rebgun as the applicant company's interim receiver. It also prohibited the company's management from disposing of any of its property exceeding RUB 30 million in value.

284. On 6 and 7 April 2006 the applicant company appealed against the decision of 29 March 2006 on all three points.

285. On 27 April 2006 the Appeal Court dismissed the appeals.

286. On 21 June 2006 the applicant company appealed against the lower courts' decisions to the Circuit Court. The outcome of these proceedings is unclear.

287. On 21 April 2006 the Ministry submitted a claim to the City Court, seeking to be included in the list of the applicant company's creditors for the amount of 353,766,625,235.66 RUB (approximately EUR 10,435,809,153),

along with 2,118 pages of documentation. The claim was based on the company's reassessed tax liability for the year 2004.

288. In June 2006 the City Court made a number of rulings concerning the formation of the list of creditors. In particular, on 1 and 7 June 2006 the City Court held hearings on the claim. On 14 June 2006 the final hearing of the claim was held. The court allowed the claims in its entirety and dismissed the application for stay.

289. On 21 June 2006 the City Court delivered a full version of the judgment of 14 June 2006. It decided to include the Ministry in the list of the applicant company's creditors for the amount claimed and refused to stay the proceedings.

290. On 3 and 6 July the applicant company appealed against the judgment of 14 June 2006 concerning the allowed claims.

291. On 4, 7 and 11 August 2006 the Appeal Court heard the applicant company's arguments.

292. On the latter date the Appeal Court dismissed the applicant company's appeal.

293. It appears that on 18 August 2006 the Appeal Court delivered a full version of the appeal decision.

294. On 25 July 2006 the Committee of Creditors rejected the rehabilitation plan offered by the management and recommended the applicant company's liquidation.

295. On 31 July 2006 the applicant company appealed against this decision.

296. On 4 August 2006 the City Court examined the applicant company's situation, declared that the company was bankrupt and dismissed its management. The court appointed Mr E. Rebgun as the applicant company's trustee. It also refused the company's request to stay the proceedings.

297. Both parties appealed on 15 August 2006

298. The judgment was upheld on appeal and entered into force on 26 September 2006.

299. It appears that on 22 August 2006 Mr E. Rebgun, acting as the trustee in the company's bankruptcy proceedings, revoked the authority of all counsel appointed by the applicant company's previous management, including Mr P. Gardner.

300. On 23 October 2006 Mr E. Rebgun appointed a consortium of independent appraisers led by ZAO Roseko ("the consortium"), selected through an open tender, to inventory and evaluate the applicant company's assets with a view to auctioning them.

301. The consortium carried out its evaluation from October 2006 to July 2007.

302. From 27 March to 15 August 2007 Mr E. Rebgun held 17 public auctions at which all of the applicant company's assets were sold in line with the evaluations which had been made earlier by the consortium. The

aggregate proceeds amounted to over RUB 860 billion (around USD 33.3 billion). The assets sold included a 20% stake in OAO Sibneft (sold, along with 12 fully owned subsidiaries, blocks of shares in 5 more entities and some exchange notes, for RUB 151.536 billion, or some EUR 4.387 billion), 9.44% of shares of OAO Rosneft (sold, along with 12 exchange notes of OAO Yuganskneftegaz, for RUB 197.840 billion, or some EUR 5.728 billion) and scores of the company's subsidiary companies.

303. By a decision of 12 November 2007, the full version of which was produced on 15 November, the City Court examined the applicant company's situation, heard the report by Mr E. Rebgun and decided to terminate the liquidation proceedings. The applicant company ceased to exist, leaving over RUB 227.1 billion (around USD 9.2 billion) in unsatisfied liabilities.

304. On 21 November 2007 a certificate was issued to the effect that the applicant company had been liquidated on the basis of the court decision.

305. It appears that a company Glendale Group Limited and Yukos Capital S.A.R.L. contested the decision of 12 November 2007 before the Appeal Court. The appeal of Glendale Group was declared inadmissible for the failure to submit it on time, whilst the appeal of Yukos Capital S.A.R.L. has been accepted for examination. The hearing in this respect was scheduled by the Appeal Court on 19 November 2007.

306. The outcome of these proceedings remains unclear.

II. RELEVANT DOMESTIC LAW AND PRACTICE

A. Tax liability

1. General provisions

307. Under Article 57 of the Constitution of Russia, everyone is liable to pay taxes and duties established by law.

308. Article 44 of the Tax Code of 31 July 1998 no. 146-FZ (as in force at the relevant time) states that an obligation to pay a tax or a duty arises, alters or ceases in accordance with that Code and other legislative acts on taxes and fees.

309. Articles 45 and 80 of the Tax Code provide that, as a general rule, taxpayers must comply with their obligation to pay a tax on their own initiative, and define a tax declaration as the written statement by taxpayers on their revenues and expenses, sources of revenue, tax benefits and the calculated sum of the tax, as well as other data related to calculation and payment of the tax.

310. Under Article 45, in the event of non-payment or incomplete payment of the tax in due time, the tax authorities may levy the tax liability directly from the taxpayer's bank account.

311. Article 11 (2) of the Tax Code defines a branch of an organisation as a geographically separate department, with stable employment posts.

2. Tax inspections

312. Under Articles 82 and 87 of the Tax Code, the tax authorities may carry out documentary and on-site tax inspections of taxpayers. Such inspections may cover only the three calendar years of the taxpayer's activity directly preceding the year of inspection. In exceptional cases the authorities are allowed to carry out repeated on-site tax inspections. Such cases include, among other things, on-site inspections conducted by way of supervision of the activities of the tax authority that conducted the initial audit (Article 87 (3) of the Code).

313. Article 101 (4) 2 of the Tax Code states that the tax authority may use as evidence during its inspections documents earlier demanded by the authority from a taxpayer, documents submitted or obtained during documentary and on-site tax inspections of that taxpayer as well as other documents in the possession of the authority.

314. Under Article 100 (5) of the Tax Code a taxpayer has two months to file a detailed reply to the report drawn up by the tax authorities on the outcome of the tax inspection.

315. Under Article 81 of the Tax Code, a taxpayer may not be fined in respect of any errors if, prior to commencement of the on-site tax inspection for the relevant year, it files amended tax returns and voluntarily satisfies the related tax liabilities, including default interest.

316. By order no. BG-3-29/159 dated 2 April 2003 the Tax Ministry decided that the period for performance of the demand to pay tax addressed to a taxpayer may not exceed ten calendar days from the date of its receipt by the taxpayer.

317. The Government relied on the following cases as examples of typical terms given to taxpayers for voluntary payment of reassessed taxes and surcharges:

(a) Case no. A82-11/2003-A/6

318. On 13 November 2000 the Tax Ministry demanded that respondent OAO Slavneft-YANOS pay reassessed taxes and interest surcharges amounting to over RUB 53 million within one day. The court decisions in the case were taken on 11 June 2003, 7 October 2003 and 19 January 2004.

(b) Case no. A33-16983/01-S3a-F02-1826/02-S1

319. On 31 May 2001 the Tax Ministry ordered the Municipal Housing and Utilities Infrastructure of the Kansk District to pay reassessed taxes in the amount of RUB 814,581.54 within one day. The first judgment of 9 April 2002 was upheld by the cassation instance on 16 July 2002.

(c) Case no. F04/1724-594/A27-2004

320. On 23 January 2003 the Tax Ministry ordered FGUP PO Progress to pay reassessed taxes in the amount of RUB 72,827,208 within one day. The court decisions were taken on 4 September, 16 December 2003 and 5 April 2004 respectively.

(d) Case no. A26-8688/03-26

321. On seven occasions in 2003 the Tax Ministry ordered OOO Krasnaya Rybka to pay reassessed taxes and interest surcharges in the overall amount of RUB 760,043.19 within one day. The first-instance judgment in the case, dated 13 February 2004, was upheld by a cassation decision of 16 June 2004.

(f) Case no. F04-2648/2005(10969-A61-37)

322. On 25 August 2004 the Tax Ministry ordered OOO YamalGIS-Servis to pay reassessed taxes in the amount of RUB 268,083 on the same day. The court decisions upholding the demand were taken on 9 December 2004, 24 February and 4 May 2005.

B. Applicable taxes

1. General provisions

323. Article 38 of the Tax Code provides that objects of taxation may be operations involving the retailing of goods, works and services, property, profit, income, value of retailed goods, works and services or other objects having cost, quantitative or physical parameters on the existence of which the tax legislation bases the obligation to pay tax.

324. Article 39 of the Code defines retailing of goods, works and services as, *inter alia*, the transfer (including exchange of services, works and goods) in return for compensation of property rights in respect of goods and results of works from one person to another, as well as the rendering of services from one person to another in exchange for compensation.

325. Article 41 of the Code defines profits as economic gains in monetary form or in kind.

2. Value-added tax

(a) Before the entry into force of the Second Part of the Tax Code on 1 January 2001

326. Section 3 of RF Law no. 1992-1 of 6 December 1991 "On Value-Added Tax" (as in force at the relevant time) subjects to VAT, among other things, the turnover generated by the retailing of goods, works and services on the territory of Russia, the rates of which range between 10% and 20%. Under section 5 of the Law, exported goods are exempt from payment of the tax. The exemption becomes effective only if the taxpayer properly justifies the claim. Until these documents are filed, the tax remains payable under the non-export rate.

327. Letter no. B3-8-05/848, 04-03-08 of the State Tax Service of Russia and the Ministry of Finance, dated 21 December 1995, stated that taxpayers were to file the following documents to justify this tax exemption: a contract concluded between the legal personality taxpayer registered in Russia with its foreign partner, proof of payment in respect of the goods, and a customs declaration bearing the appropriate stamp of the customs body, confirming the export of goods from the customs territory of Russia.

(b) After the entry into force of the Second Part of the Tax Code on 1 January 2001

328. In respect of VAT, the applicable tax rate is 0% if the traded goods are placed in an "export" customs regime and physically removed from the customs territory of the Russian Federation (Article 164 (1) of the Tax Code). In addition, the taxpayer may claim a refund of the "incoming" VAT already paid in respect of the exported goods.

329. For the zero rate to become effective and in order to claim the VAT refund, it is necessary to justify the claim by filing the following documents with the tax authorities (Article 165 of the Tax Code): the export contract concluded between the taxpayer and the foreign buyer, a bank statement confirming receipt of funds from the foreign buyer by a Russian bank duly registered with the tax authorities, a relevant customs declaration bearing the stamp of the customs bodies confirming the export of the goods from the customs territory of Russia, and copies of relevant transport bills and shipping documents, bearing the stamps of the customs bodies, confirming the export of goods from the customs territory of Russia.

330. On 14 July 2003 the Constitutional Court issued ruling no. 12-P, in which it essentially upheld the constitutionality of Article 165 of the Code. The court distinguished between documents required by public-law norms, such as the taxpayer's customs declaration bearing the relevant stamps from the customs bodies, and which are mandatory in all cases, and other documents such as contracts, transport bills etc. In view of the different practices of the economic actors, which made the latter type of documents

mutually replaceable, the authorities were constitutionally permitted to require a taxpayer to file these documents, but without an excessive degree of formalism.

331. The relevant documents are to be filed with the competent tax authority within 180 days from the date of the customs clearance of the goods in question (Article 165 (9) of the Tax Code). Until these documents are filed, the tax remains payable under the non-export rate. A taxpayer is not precluded from filing the documents in question even after the expiry of the time-limit in question (Article 176 of the Tax Code).

332. By a decision of 28 April 2003 (case no. F09-1159/03-AK) in the case of ZAO Aktsionernaya neftyanaya kompaniya v. the Tax Ministry, the Federal Commercial Court of the Ural District, acting as a cassation review court, rejected the company's claims for VAT refunds with reference to its failure to satisfy the requirements of Article 165 of the Code. The company could not prove the fact of actual payment for the allegedly exported goods.

333. By a decision of 17 February 2004 (case no. F09-187/04-AK) in the case of OOO Firma Galaktika v. the Tax Ministry, the Federal Commercial Court of the Ural District, acting as a cassation review court, rejected the company's claims for VAT refunds with reference to its failure to satisfy the requirements of Article 165 of the Code. The company failed to submit a proper bank statement confirming receipt of funds from the foreign buyer.

334. By a decision of 3 May 2005 (case no. A56-31805/04) in the case of ZAO Stroitelnyy trest no. 28 v. the Tax Ministry, the Federal Commercial Court of the North Western District examined the decisions of lower courts whereby the company had been refused VAT refunds at first instance (by a judgment of 11 October 2004 – the company failed to submit the properly stamped customs declaration confirming the actual export of the goods) and had subsequently been granted them on appeal (by a decision of 21 January 2005 – the appeal court decided that the fact of the actual export had been established by a final court decision in a related court dispute). The cassation court quashed the appeal decision, having noted that the requirements set out in Article 165 of the Code were strict and unequivocal and that the law did not allow for any replacement of the customs declaration by other means of proof.

335. By a decision of 9 March 2005 (case no. F09-563/05-AK) in the case of OAO Kachkanarskiy gorno-obogatitelnyy kombinat Vanadiy v. the Tax Ministry, the Federal Commercial Court of the Ural District quashed the decisions of lower courts whereby the company had been granted VAT refunds. The cassation court noted that the requirements set out in Article 165 of the Code were strict and unambiguous and that the law required the taxpayer to prove the actual export solely by means of the properly stamped customs declaration, which had not been done by the company in the present case. Accordingly, the court rejected the company's claims.

336. By a decision of 27 September 2005 (case no. F09-4252/05-C2) in the case of OAO Nauchno-proizvodstvennyy centr vysokotochnoy tekhniki Izhmash v. the Tax Ministry, the Federal Commercial Court of the Ural District, acting as a cassation review court, rejected the company's claims for VAT refunds with reference to its failure to satisfy the requirements of Article 165 of the Code in a timely manner, that is, within six months.

3. Motorway fund tax

337. Section 5 (2) of RF Law no. 1759-1 of 18 October 1991 "On motorway funds in the Russian Federation" provides for a 1% motorway users' tax from the turnover of the retail of goods, works and services, payable by all motorway users. Section 4 also makes subject to a 25% tax the turnover (excluding VAT) of companies trading in fuels and lubricants.

338. This tax was abolished from 1 January 2003.

4. Tax for the maintenance of the housing stock and socio-cultural facilities

339. Section 21 ("Ch") of RF Law no. 2118-1 of 27 December 1991 "On the foundations of the tax system" imposes a tax of up to 1.5% for the maintenance of the housing stock and socio-economic facilities.

340. This tax was abolished with the entry into force of the Second Part of the Tax Code on 1 January 2001.

5. Corporate property tax

(a) Before the entry into force of the Second Part of the Tax Code on 1 January 2001

341. Section 2 (1-2) of RF Law no. 2030-1 of 13 December 1991 "On corporate property tax" provided for a tax of up to 2% in respect of organisations' property.

(b) After the entry into force of the Second Part of the Tax Code on 1 January 2001

342. Chapter 30 of the Tax Code provides for a tax of up to 2.2% in respect of organisations' property. The exact rate is defined by the regional authorities.

6. Profit tax

(a) Before the entry into force of the Second Part of the Tax Code on 1 January 2001

343. Law no. 2116-1 of 27 December 1991 "On profit tax on enterprises and organisations" (sections 2 and 5) provided for a profit tax, the rate of

which could vary depending on the type of taxable activity and the rate fixed by the local authorities. The mandatory rate to be transferred to the Federal budget was 11%.

(b) After the entry into force of the Second Part of the Tax Code on 1 January 2001

344. Chapter 25 of the Tax Code provides for a profit tax of up to 24% (6.5% to be transferred to the Federal budget and the rest to the regional budget).

7. Advertising tax

345. Section 21 (1) "z" of RF Law no. 2118-1 of 27 December 1991 "On the foundations of the tax system" imposed a tax in respect of the cost of advertisement services.

346. This tax was abolished from 1 January 2005.

C. Tax advantages

1. General provisions

347. Article 56 of the Tax Code defines a tax benefit as a full or partial exemption from the payment of taxes, granted by the tax legislation.

348. In letter no. 04/06/08, dated 21 October 1998, the Ministry of Finance noted, *inter alia*:

> "...[that] experience in creating and operating free economic zones in the Russian Federation, established pursuant to both federal laws (the special economic zone in the Kaliningrad region) and resolutions of the authorities of constituent entities of the Federation (Kalmykiya, Tuva), [has] demonstrate[d] that the creation of such zones across such vast areas in the absence of a proper analysis of investment projects leads to abuses of the tax and customs incentives granted and, accordingly, to serious losses suffered by the federal and local budgets, as reported by the Ministry of Finance of Russia to the Government of Russia on multiple occasions."

2. Requirements relating to the registration of taxpayers

349. Under Article 83 (1) of the Tax Code, taxpayers which are legal entities are required to register with the tax authorities at their headquarters (location of their executive bodies), at the location of their branches and at the location of any real estate and places where vehicles belonging to them are registered.

350. Special registration rules applied in respect of large taxpayers, including the applicant company.

351. By Decree no. АП-3-10/399 of the Tax Ministry, dated 15 December 1999, such taxpayers are required to register at their main

location, at the location of their branches and at the location of real estate and places where vehicles belonging to them are registered, and in certain specific tax offices (inter-district level or as specifically indicated by the Ministry).

352. Annex 3 to the Decree contains the form "On subsidiary and dependant companies and subsidiary enterprises", to be filled in by the taxpayer. During registration the taxpayer is required to indicate all of its subsidiary and dependant companies.

353. In respect of domestic off-shore territories, according to commentators, this requirement means that in practice the taxpayer's executive body should always be physically located and functioning on the territory of the off-shore. If the taxpayer fails to comply with the requirement, the tax authorities could declare its registration void with the subsequent recovery of the entirety of the perceived tax benefits (see A.V. Bryzgalin, *Practical Tax Encyclopaedia*, Moscow, 2003-2006, Chapter 3 "Methodology of tax optimisation").

3. Closed administrative-territorial formations (the town of Sarov in the Nizhniy Novgorod Region, the town of Trekhgornyy in the Chelyabinsk Region and the town of Lesnoy in the Sverdlovsk Region)

(a) Legal provisions

354. Under section 5 of Law no. 3297-1 of the Russian Federation "On closed administrative-territorial formations", tax concessions are provided to businesses if, *inter alia*, they have at least 90% of their fixed assets and conduct at least 70% of their activities on the territory of the respective formation (including a requirement that at least 70% of their employees be made up of persons permanently residing in the ZATO in question, and that at least 70% of their wage bill be paid to employees permanently residing in that territory).

355. Letter no. АП-6-01/505 of the Tax Ministry, dated 24 June 1999, contained Methodological Directions to the tax bodies on issues concerning the lawfulness of the use of additional tax benefits granted by local authorities in the closed administrative-territorial formations. It stated that the tax authorities ought to verify the actual presence of the taxpayer's assets on the territory in question by checking its accounting records and financial statements, and by confirming the physical location of the organisation at the indicated address and the fact of genuine performance by the taxpayer's employees at the taxpayer's registered location.

(b) Case no. A42-6604/00-15-818/01 (The Tax Ministry v. OOO Pribrezhnoe), referred to by the applicant company

356. The respondent legal entity was OOO Pribrezhnoe, registered in the closed administrative territorial formation town of Snezhnogorsk, which has a privileged tax regime. The Ministry tried unsuccessfully to contest the use of tax concessions by the respondent, by demonstrating that the entity had not been actually present at the place of its registration. The domestic court found for the respondent. They established that the entity had some assets on the territory of Snezhnogorsk, a number of permanent employees (including a lawyer and the cleaning lady), and a cash account in the local bank, which proved that the entity satisfied the criteria provided for in law.

357. The final decision in the case was taken by the Court of Cassation on 5 June 2002.

4. The Republic of Mordoviya

358. Under Law no. 9-FZ of the Republic of Mordoviya of 9 March 1999 "On the conditions of efficient use of the socio-economic potential of the Republic of Mordoviya", tax concessions are granted to taxpayers whose entities were established after the entry into force of that law and whose activities meet certain conditions, including but not limited to the following:

(a) they conduct export operations, the quarterly proceeds from which account for at least 15%of the business's total earnings;

(b) they engage in wholesale trade in fuel and lubricants and other types of hydrocarbon raw materials, the quarterly proceeds from which account for at least 70% of the business' total earnings.

359. Section 1 of the Law states that "this Law establishes concessions with the objective of creating favourable conditions for attracting capital into the territory of the Republic of Mordoviya, strengthening the socio-economic potential of the Republic of Mordoviya, developing the securities market and creating new jobs through special arrangements for the taxation of organisations".

5. The Republic of Kalmykiya

360. Law no. 12-P-3 of the Republic of Kalmykiya of 12 March 1999 "On tax concessions for companies investing in the Republic of Kalmykiya" provides tax concessions to those who meet the following criteria:

(a) the taxpayer is not a user of mineral resources in the territory of the Republic;

(b) the taxpayer is registered with the Ministry of Investment Policy of the Republic of Kalmykiya as an enterprise investing in the economy of the Republic;

(c) the enterprise's investment in the economy of the Republic meets the criteria established by the Ministry of Investment Policy of the Republic in accordance with this law.

361. By a decision of 16 April 2002 (case no. F08-1134/2002-402) in the case of OOO Simpleks v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

362. By a decision dated 29 April 2002 (case no. F08-1368/2002-506A) in the case of OOO Impuls v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and indeed made any investments in the local economy.

363. By a decision of 20 May 2002 (case no. F08-1678/2002-614A) in the case of OOO Sibirskaya transportnaya kompaniya (one of the sham entities belonging to the applicant company) v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District ruled as follows:

> "[b]ased on the content and meaning of the [above-mentioned] law and Resolution no. 7 of the Elista Town Administration, [the purpose of the municipal legislation] is to attract funds from various investors for development of the regional and local economies, given the lack of funds in the regional and local budgets and the need for their replenishment to ensure the activities of the Kalmyk Republic and the town of Elista ...
>
> The case documents show that RUB 27,196 came from the plaintiff for development of the regional and local economies, whereas RUB 6,918,617 did not enter the regional and local budgets directly. Thus, the investments made by [OOO Sibirskaya transkportnaya kompaniya] amount to 0.4% of the amount of taxes that would otherwise have been payable by it. They have no effect on the development of the economy [and] do not cover the budgetary losses related to the granting of incentives to taxpayers; on the contrary, they have consequences in the form of unfair enrichment at the expense of budgetary funds. Thus, given that the amount of the investments made by the plaintiff is incommensurate to the amount of incentives used, the plaintiff abused its right, that is, it acted in bad faith".

Accordingly, the court quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had complied with the above-mentioned conditions and whether it had acted in good faith.

364. By a decision of 28 May 2002 (case no. F08-1793/2002) in the case of ZAO Telekom Zapad Komplekt v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District ruled that:

> "[b]ased on the meaning and contents of the [above-mentioned] law and Resolution no. 7 of the Elista Town Administration, it follows that [the purpose of the municipal legislation] is to attract funds from various investors for development of the regional and local economies, given the lack of funds in the regional and local budgets and the

> need for their replenishment to ensure the activities of the Kalmyk Republic and the town of Elista...
>
> ... [the court has to examine] the proportion between the investments made by the [taxpayer] and the amount of tax that did not enter the budget [in order] to resolve the issue of the plaintiff's good faith and its abuse of its rights".

Accordingly, the court quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had complied with the above-mentioned conditions and had acted in good faith.

365. By a decision of 4 June 2002 (case no. F08-1864/2002-697A) in the case of ZAO Promyshlennaya korporaciya Shar v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

366. By a decision of 5 August 2002 (case no. F08-2762/2002-1009A) in the case of OOO Promet v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

367. By a decision of 13 August 2002 (case no. F08-2892/2002-1051A) in the case of OOO TD Dion v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

368. By a decision of 29 August 2002 (case no. F08-3158/2002-1140A) in the case of ZAO Stanford v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

369. By a decision of 20 February 2003 (cases nos. F08-270/2003-91A and F08-1679/2002-622A) in a dispute between the Tax Ministry and OOO "Vostochnaya perestrakhovochnaya kompaniya", the Federal Commercial Court of the North-Caucasian Circuit found as follows:

> "The investments made by the [taxpayer] amount to 0.14% of the amount of taxes that would otherwise have been payable by it. They have no effect on the development of the economy... but ... their effect is unfair enrichment .... Therefore,

> [as] the amount of investments by [the taxpayer] was incommensurate to the amount of the benefits received, [the taxpayer] abused its right, that is, it acted in bad faith"

370. By a decision of 20 February 2003 (case no. F08-268/2003-98A) in the case of OOO Bazis Sekyuritis v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

371. By a decision of 8 April 2003 (case no. F08-1013/2003-383A) in the case of OOO Gravite v. the Tax Ministry, the Federal Commercial Court of the North-Caucasian District quashed the decisions of the lower courts and instructed them to investigate further whether the taxpayer had indeed complied with the conditions mentioned in the law, had acted in good faith in this respect and had indeed made any investments in the local economy.

6. The Evenk Autonomous District

372. Under section 9 of Law no. 108 of the Evenk Autonomous District "On specific features of the tax system in the Evenk Autonomous District" of 24 September 1998, substantially lower tax rates apply to local businesses whose activities meet certain conditions with regard to the special taxation procedure set out in section 8 of that Law.

D. The use and interpretation of terms of civil legislation in tax disputes

373. Under Article 11 of the Tax Code, the institutions, notions and terms of the civil legislation of Russia used in the Tax Code keep their respective meanings, unless specifically stated.

E. General principles governing the status of legal entities

1. Presumption of independence

374. Under Article 2 of Civil Code of 30 November 1994 no. 51-FZ (as in force at the relevant time), the legal status of parties involved in civil-law transactions, the grounds for the creation of ownership and other property rights and the order of exercising those rights are defined by the civil legislation, which also regulates contractual and other obligations.

375. The civil legislation regulates the relations between persons engaged in business activities or in those activities performed with their participation, on the assumption that business activity is an independent activity performed at one's own risk and aimed at systematically deriving a

profit from the use of property, the sale of commodities, the performance of work or the rendering of services by those persons registered in this capacity in conformity with the legally-established procedure.

376. It is formally prohibited to make any unilateral property transfers (gifts, grants or gratuitous loans) between independent commercial legal entities (Articles 575 and 690 of the Civil Code). Unilateral property transfers are permitted by Article 251 (1) 11 of the Tax Code and not counted for the purposes of profit tax if they are made between associated entities, where one of them holds more than 50% of shares in the equity of the other entity.

2. Rules applicable to subsidiary and dependant companies

377. Article 105 of the Civil Code provides that a subsidiary company is one controlled by another company, either through ownership of the subsidiary company's shares, by virtue of a contract or by any other means.

378. The controlling company is jointly responsible for debts incurred by the subsidiary company as a result of compliance with the controlling company's instructions. The controlling company may be held vicariously responsible for a debt of the subsidiary company in the event of the latter's insolvency.

379. Article 106 of the Code provides that a company is dependant when the other company owns over 20% of the first company's voting stock. A company which purchases over 20% of the voting shares in other companies is obliged to make this information public.

380. Similar rules are established in respect of limited liability companies (*общества с ограниченной ответственностью*) by section 6 of Law no. 14-FZ on limited liability companies of 8 February 1998.

F. Definition of a property owner

381. Article 209 of the Civil Code defines an owner as the person who has the rights of possession, use and disposal of his property. In respect of this property, the owner is entitled, at his will, to perform any actions not contradicting the law and the other legal acts, and not violating the rights and legally protected interests of other persons.

G. Contractual freedom and its limits

1. Presumption of good faith and prohibition on abuse of rights

382. Articles 9 and 10 of the Civil Code provide that the parties involved in civil-law transactions are free to act contractually within the limits defined by law.

383. Article 10 (1 and 2) of the Code states specifically that parties involved in civil-law transactions are prohibited from abusing their rights. In such cases, the courts may deny legal protection in respect of the right which is being abused. Article 10 (3) establishes a refutable presumption of good faith and reasonableness of actions on the parties in civil-law transactions.

2. Examples of the case-law of the domestic courts concerning the notion of bad faith

384. In its decision no. 24-P dated 12 October 1998, the Constitutional Court of Russia for the first time made use and interpreted the notion of "bad/good faith" to assess the legal consequence of the conduct of taxpayers in its jurisprudence. In this case this was done to define the moment at which a taxpayer can be said to have discharged his or her constitutional obligation to pay taxes.

385. In its decision no. 138-O dated 25 July 2001, the Constitutional Court of Russia again confirmed that there existed a refutable presumption that the taxpayer was acting in good faith and that a finding that a taxpayer had acted in bad faith could have unfavourable legal consequences for the taxpayer. The case again concerned the definition of a moment at which a taxpayer can be said to have discharged his or her constitutional obligation to pay taxes.

386. The domestic commercial courts applied this approach in a number of cases concerning the eligibility of taxpayers to tax concessions in the Republic of Kalmykiya, such as decision no. F08-1134/2002-402 of 16 April 2002 of the Federal Commercial Court of the North Caucasian Circuit, decision no. F08-1864/2002-697A of 4 June 2002 of the Federal Commercial Court of the North Caucasian Circuit, decision no. F08-2762/2002-1009A of 5 August 2002 of the Federal Commercial Court of the North Caucasian Circuit, decision no. F08-2892/02-1015A of 12 August 2002 of the Federal Commercial Court of the North Caucasian Circuit, decision no. F08-3158/2002-1140A of 29 August 2002 of the Federal Commercial Court of the North Caucasian Circuit, decision no. F08-268/2003-98A of 20 February 2003 of the Federal Commercial Court of the North Caucasian Circuit, decision no. F08-1013/2003-383A of 8 April 2003 of the Federal Commercial Court of the North Caucasian Circuit.

387. In its decision no. 168-O of 8 April 2004 the Constitutional Court noted that it would be inadmissible for bad-faith taxpayers to manipulate the legal civil-law institutions to create and operate schemes for unlawful enrichment at the expense of the State budget. The case concerned the use of exchange notes in the sphere of VAT refunds.

3. Rules governing sham transactions

(a) Statutory law

388. Under Article 153 of the Civil Code, transactions are defined as activities of natural and legal persons creating, altering and terminating their civil rights and obligations.

389. Article 166 of the Civil Code states that a transaction may be declared invalid on the grounds established by that Code, either by force of its being recognized as such by the court (a voidable transaction, *оспоримая сделка*), or regardless of such recognition (a void transaction, *ничтожная сделка*).

390. Under Article 167 of the Civil Code, void transactions entail no legal consequences, apart from those relating to their invalidity, and are invalid from the moment they are conducted.

391. Article 170 (2) establishes specific rules in respect of two types of void transactions: 'imaginary' transactions ("*мнимая сделка*", effected only for form's sake, without the intention to create the corresponding legal consequences) and 'sham' transactions ("*притворная сделка*", which are effected for the purpose of screening other transactions). This provision condemns both imaginary and sham transactions as void.

392. It also provides that in the event of sham transactions, the rules governing the transaction that was in fact intended by the parties may be applied by a court, regard being had to the substance of this transaction (the so-called "substance over form" rule).

393. Under Article 45 (2) 3 of the Tax Code the power to re-characterise transactions by a taxpayer with third parties, their legal status and the nature of the taxpayer's activity in tax disputes lies with the courts (as opposed to executive bodies). Section 7 of Law no. 943-1 of 21 March 1991 "On Tax Authorities in the Russian Federation" vests the power to contest such transactions and recover everything received in such transactions with the State budget.

(b) Academic sources

394. Comments on the Civil Code (O.N. Sadikov, *Comments on the Civil Code*, Yuridicheskaya firma Kontrakt Infra-M, Moscow, 1998) states, with reference to Bulletin no. 11 of the Supreme Court of RSFSR (page 2), that any evidence admitted by the rules on civil procedure may also serve as proof of the invalidity of sham transactions.

H. General rules on price formation and the price adjustment mechanism

395. Article 40 (1) of the Tax Code requires that the parties trade at market prices. It also establishes a refutable presumption that the prices agreed to by the parties correspond to market levels and are used for taxation purposes.

I. Price adjustment mechanism of the Tax Code

396. Under Article 40 (2) of the Tax Code, the tax authorities are empowered to overrule the above presumption by verifying and correcting the prices for taxation purposes. A finding that the prices were lowered usually leads to the conclusion that the taxpayer understated the taxable base and thus failed properly to pay his taxes (see Article 122 of the Tax Code below).

397. This may happen only (1) when the parties are interdependent within the meaning of Article 20 of the Tax Code; (2) in the event of barter transactions, or; (3) international transactions; (4) when the prices set by a taxpayer during the same short period for certain identical types of goods, work or services fluctuate by more than 20%.

398. Article 20 (1) of the Tax Code defines interdependent parties as natural persons and (or) organisations whose mutual relations may influence the terms or economic results of their respective activities or the activities of the parties that they represent. In particular, (a) one organisation has a direct and (or) indirect interest in another organisation, and the aggregate share of such interest is more than 20%. The share accounted for by the indirect interest held by one organisation in another, through a chain of separate organisations, is defined as the product of the direct interest shares that the organisations in this chain hold in one another; (b) one natural person is subordinate to another natural person *ex officio*; (c) in the case of individuals, they are spouses, relatives, adopters or adoptees, guardians or wards under the family law of the Russian Federation.

399. Article 20 (2) of the Tax Code provides that the court may recognize persons as interdependent on other grounds, not provided for by Item 1 of that Article, if the relations between these persons may have influenced the results of transactions in the sale of goods (work, services).

J. Applicable tax offences and related penalties

400. Article 122 §§ 1 and 3 of the Tax Code imposes a penalty of 40% of the unpaid tax liability on intentional non-payment or incomplete payment of the tax due, as a result of understating the taxable base. Articles 112 § 2 and 114 § 4 of the Tax Code provide for a 100% increase in this penalty in

the event of a repeated offence by the same taxpayer. Article 114 § 3 of the Code also provides for a possibility of reducing the fine by half if there were extenuating circumstances on the facts of the case.

401. Article 114 § 7 of the Code makes it mandatory to recover the penalties in court. This rule does not apply to reassessed fines and interest surcharges.

402. Article 75 of the Tax Code provides for payment of an interest surcharge by taxpayers in cases of late payment of the taxes due. The interest surcharge amounts to one three-hundredth of the statutory rate for each day of the delay. Persons and entities that were unable to meet their tax liabilities in due time because their bank account was suspended by the tax authority or a court are excused from payment of the interest surcharge for the duration of the respective suspension (Article 75 § 3 of the Tax Code).

K. Statutory time-bar

1. Situation prior to the Constitutional Court's decision of 14 July 2005

(a) Statutory law

403. In accordance with Article 113 § 1 of the Tax Code (Chapter 15 General provisions concerning liability for tax offences), a person could not be held liable for a tax offence under Article 122 of the Code if three years had expired since the first day after the end of the tax period during which the offence was committed. The above provision only applied to the payment of fines. Article 115 of the Code sets out an additional six-month time-limit within which the authorities must collect the fines. It starts running from the date of adoption of the relevant audit report.

404. As regards the reassessed taxes and interest surcharges, Article 87 of the Tax Code (as in force as the relevant time) limited the ability of the authorities to carry out tax inspections by stating that "the[y] ... [may] only be carried out in respect of the activities of the relevant taxpayer ... during the three calendar years immediately preceding the year of the tax inspection" (see also decision no. 3803/01 of the Supreme Commercial Court below).

(b) Practice directions by the Supreme Commercial Court

405. In paragraph 36 of Resolution of the Plenum of the Supreme Commercial Court no. 5 dated 28 February 2001 "On certain issues arising from application of the first part of the Tax Code", the court indicated to the lower courts that "a taxpayer is considered to have been held liable [within the meaning of Article 113 of the Tax Code] on the date on which the head

of the [relevant] tax body or his deputy takes a decision to hold this person liable of a tax offence in accordance with [the rules set out in] the Code".

406. This interpretation was subsequently used by the Presidium of the Supreme Commercial Court in its decision no. 3803/01 (Averyanov v. the Tax Ministry), taken in 2002, where an offence had been committed in 1996, whilst the time-limit began to run on 1 January 1997 and expired on 1 January 2000. The Ministry's decision was issued on 25 January 2000 and was, accordingly, time-barred in so far as the fines were concerned.

(c) Case no. F09-3155/05-AK (OAO Bashselstroy v. the Tax Ministry)

407. On 30 September 2003 the Federal Commercial Court of the Ural Circuit reviewed and quashed the lower courts' decisions in a tax dispute involving the Tax Ministry and a private shareholding. Among other things, the Circuit Court stated that the time-limit set out in Article 113 of the Code started running from the date on which the relevant facts came to the attention of the competent authorities (as a result of a tax inspection or other types of tax control).

(d) Cases referred to by the applicant company

408. In a number of cases pre-dating the decision of the Constitutional Court of 14 July 2005, the courts applied Article 113 in line with an interpretation given by Resolution no. 5 of the Plenum of the Supreme Commercial Court of 28 February 2001 (see decision no. F04/7-1527/A27-2002 of 4 January 2003 of the Federal Commercial Court of the Western Siberia Circuit, decision no. F04/7-1527/A27-2002 of 8 January 2003 of the Federal Commercial Court of the Northern Western Circuit, decision no. F03-A59/03-2/745 of 23 April 2003 of the Federal Commercial Court of the Far-Eastern Circuit, decision no. A48-1188/03-2 of 12 November 2003 of the Federal Commercial Court of the Central Circuit, decision no. A82-471/2004-8 of 8 October 2004 of the Federal Commercial Court of the Volgo-Vyatskyy Circuit, decision no. F03-A73/04-2/947 of 19 May 2004 of the Federal Commercial Court of the Far Eastern Circuit, decision no. A19-3142/04-40-F02-3338/04-C1 of 24 August 2004 of the Federal Commercial Court of the Eastern Siberia Circuit, decision no. A19-9731/03-15-F02-4732/03-C1 of 9 January 2004 of the Federal Commercial Court of the Eastern Siberia Circuit, decision no. A33-15117/03-C3-F02-1877/04-C1 of 2 June 2004 of the Federal Commercial Court of the Eastern Siberia Circuit, decision no. KA-A41/9494-04 of 20 October 2004 of the Federal Commercial Court of the Moscow Circuit, decision no. F09-4221/04AK of 13 October 2004 of the Federal Commercial Court of the Ural Circuit, and decision no. F09-3799/04AK of 4 September 2004 of the Federal Commercial Court of the Ural Circuit). None of these cases involved a situation whereby a taxpayer had hindered a tax inspection or had deliberately sought to delay the tax proceedings.

2. Situation after the Constitutional Court's decision of 14 July 2005

(a) Case no. KA-A40/5876-06 (OAO Korus-holding v. the Tax Ministry)

409. By a decision of 28 July 2006 the Federal Commercial Court of the Moscow Circuit, acting as a cassation review instance, reviewed the application of the time-limits of Article 113 of the Code. The audit report prepared by the Ministry in respect of the calendar year 2001 was dated 28 February, whilst the decision to hold the taxpayer liable was issued on 29 March 2005. The Circuit Court decided that the authorities could be said to have been acting in time provided that they respected the requirements of Article 87 of the Code, which sets out a three-year time-limit for conducting tax inspections and Article 23 § 8 (1) of the Code, which sets out a four-year time-limit for the maintenance of accounting documents. The Circuit Court also specifically noted the actions of OAO Korus-holding, which had sought to hinder and complicate the tax inspection.

(b) 2006 amendments to Article 113 of the Tax Code

410. The text of Article 113 has been amended by Federal Law no. 137-FZ of 27 July 2006, which came into force on 1 January 2007. The provision now contains § 1.1., which states:

> "1.1. The running of the time-limit for holding a taxpayer liable stops if [the taxpayer] actively hindered an on-site tax inspection, thus creating an insurmountable obstacle for that inspection and for the determination by the tax authorities of the amount of taxes due to the budgetary system of the Russian Federation.
>
> The running of the time-limit [in question] is suspended on the date of adoption of a report [setting out the circumstances in which the taxpayer denied the tax authorities access to the relevant documents]. In this case, the running of the time-limit continues on the date when the above-mentioned circumstances no longer exist and a decision on continuation of the on-site tax inspection is taken."

(c) Case no. F08-2786/2007-1290A (the Tax Ministry v. N. A. Borshcheva)

411. On 31 May 2007 the Federal Commercial Court of the North Caucasian Circuit, acting as a cassation review instance, reviewed the application of the time-limits of Article 113 of the Code. The audit report prepared by the Ministry in respect of the calendar years 2001-2004 was dated 18 July 2006, whilst the decision to hold the taxpayer liable was issued on 4 September 2006. Again, the Circuit Court decided that the authorities had been acting in time, regard being had to the taxpayer's actions for the purpose of delaying and hindering the tax inspection.

L. Applicable rules on court procedure

1. First-instance proceedings

(a) Territorial jurisdiction

412. Under Article 35 of the Code of Commercial Court Procedure of 24 July 2003 no. 95-FZ (as in force at the relevant time), claims should be brought to a court having jurisdiction over the defendant's official place of business.

413. Article 54 of the Civil Code defines a company's official place of business as the place of the company's registration, unless, in accordance with the law, the company's articles of association do not specify otherwise.

414. Decision no. 6/8 of the Plenary Session of the Supreme Court and Supreme Commercial Court of 1 July 1996 specifies that the company's official place of business is the location of its entities.

(b) Interim measures

415. Under Article 91 of the Code of Commercial Court Procedure, a party may apply for proportionate security measures, including attachment of a defendant's assets, pending the examination of the case by the courts.

(c) Grace period

416. Article 213 of the Code of Commercial Court Procedure provides that in tax cases a court suit may be filed by the authorities when their demands have not been complied with voluntarily, or when the term for voluntary compliance has expired.

(d) Time-limits for examination of cases concerning mandatory payments and penalties

417. Article 215 of the Code of Commercial Court Procedure sets out a two-month time-limit during which a first-instance court is to finalise the examination on the merits of any case which involves mandatory payment and related penalties.

(e) Time-limits for the preparation and examination of the case at first instance

418. Article 134 of the Code of Commercial Court Procedure establishes a two-month time-limit for the preparation of the case for examination at first instance.

419. Pursuant to Article 152 of the Code, the first-instance court should examine the case and deliver its judgment within one month of a decision to list the case for a hearing.

(f) Rules on adding evidence to the case after the beginning of the hearing

420. Article 65 (3) of the Code of Commercial Court Procedure makes it mandatory for a party to disclose all evidence relied upon in their claims or objections prior to the beginning of the hearings in a case.

421. In paragraph 35 of Information Letter no. 82, dated 13 August 2004, the Supreme Commercial Court gave the following recommendation in respect of whether the trial court ought to accept and examine evidence that was previously undisclosed by the parties prior to the beginning of the hearings in a case:

> "Any evidence undisclosed by the parties to the case prior to the hearing, but submitted later during the examination of the evidence, shall be examined by the commercial court at first instance regardless of the reasons for which the procedure for disclosure of evidence was breached ..."

(g) Right to lodge an appeal against the first-instance judgment

422. Under Articles 257 and 259 of the Code of Commercial Court Procedure participants in the proceedings have one month from the delivery of the first-instance judgment to lodge an appeal.

2. Appeal proceedings

423. Under Article 267 of the Code of Commercial Courts Procedure, an appeal court must examine an appeal lodged against the first-instance judgment within one month, starting from the date of its filing. This term includes any time necessary for case preparation and for reaching the appeal decision. By federal law no. 205-FZ dated 19 July 2009 the time-limit was increased to two months. By federal law no. 69-FZ dated 30 April 2010 the provision in question has been amended. The time-limit became extendable up to six months depending on the complexity of the case and the number of participants. The provision also made it clear that the time-limit started running on expiry of the time-limit for lodging an appeal.

424. Under Article 268 of the Code, an appeal court fully re-examines the case using the evidence contained in the case and any newly-presented additional evidence. In examining procedural motions by the parties, including requests to call and hear additional witnesses or adduce and examine additional pieces of evidence, the appeal court is not bound by previous refusals of the same motions by the first-instance court.

425. Under Articles 180, 271 and 318 of the Code, the first-instance judgment becomes enforceable on the date of the entry into force of the appeal decision confirming it. The enforcement takes place on the basis on a writ issued by the respective court.

3. Cassation proceedings

426. In accordance with Article 286 of the Code, a cassation instance court, among other things, reviews the lower courts' decisions and verifies whether the conclusions of the lower courts in respect of both law and fact correspond to the circumstances of the case.

427. Article 283 of the Code provides for a possibility of applying for a stay of enforcement of the lower courts' decisions. The applicant must show that it would be impossible to reverse the effects of an immediate enforcement of the lower courts' decisions if the cassation appeal were successful.

M. Domestic courts' case-law

428. In its rulings no. 7-P dated 6 June 1995, no. 14-P dated 13 June 1996 and no. 14-P dated 28 October 1999, the Constitutional Court formulated and reiterated the principle that the constitutional right to judicial protection could not be respected unless courts examined in substance the factual circumstances of the case, without merely limiting themselves to formalistic application of the legal norms. It has frequently referred to this principle in subsequent rulings.

1. Court disputes involving re-characterisation of sham arrangements

(a) Case no. A40-31714/97-2-312 (the Tax Ministry v. OOO TF Grin Haus)

429. In 1996 the respondent legal entity was involved in a series of intertwined transactions (rent contracts and loan agreements) with two third parties: as a result, the respondent leased a building in central Moscow to the third parties, but was able to avoid inclusion of the rent payments in the taxable base of its operations by claiming that they were interest payments in respect of the loan agreement. The Ministry discovered the tax evasion scheme, re-characterised the transactions in question as rent and ordered the taxpayer to pay RUB 2 billion in back taxes.

430. The case was examined in three rounds of court proceedings by the courts at three levels of jurisdiction. Having regard to the substance of the transactions entered into by the respondent, the terms of payment and execution of the contested contracts, and, generally, to the conduct of the respondent company and the third parties, the courts decided that the contractual arrangement had been sham, re-characterised the arrangement as rent and upheld the Ministry's decision.

431. In the first round of proceedings the courts adopted their decisions on the following dates: 1 December 1997, 27 January 1998 and 30 March 1998.

432. In the second round of proceedings the decisions were adopted by the first-instance and appeal courts on 26 May 1998 and 21 July 1998. The decision of the cassation court was taken on an unspecified date.

433. The third round of proceedings involved decisions on 17 November 1998, 25 January 1999 and 2 March 1999.

(b) Case no. KA-A40/2183-98 (the Tax Ministry v. AuRoKom GMBH)

434. The respondent legal entity entered into a loan agreement with a third party; the tax authorities considered it a sham, re-characterised it as a rent contract and reassessed the tax due in respect of the profits made. The lower courts disagreed and quashed the tax authority's decision. By a decision of 17 September 1998 the cassation court quashed the lower courts' decisions and ordered that the matter be re-examined, giving due regard to all relevant circumstances, including the substance of the transaction. The courts were to reconsider all relevant clauses in the agreement in question, the conduct of the parties and the fact of physical occupation of the allegedly rented space.

(c) Case no. A40/36819/04-75-387 (the Tax Ministry v. OAO AKB Rossiyskiy Kapital)

435. The respondent legal entity is a bank which in 2001-2002 conducted business by buying and then reselling precious metals. To avoid the payment of full VAT on its sales operations in this respect, the bank entered into commission agreements with the sellers from which it bought the metals, in order to be considered not as the owner of the traded goods, but merely as the sellers' agent.

436. The domestic courts took account of the substance of the bank's transactions (terms of payment, actual circumstances of delivery and other relevant factual details) and, having established that in reality the bank had been buying and reselling the precious metals, re-characterised the bank's activity as sales. The courts referred to Article 209 of the Civil Code (containing the legal definition of an owner) and concluded that the bank first bought the precious metals, thus becoming the "owner" within the meaning of the said provision and thereafter resold the goods. They found the bank liable for tax evasion under Article 122 of the Tax Code, ordered it to pay reassessed VAT in the amount of RUB 1,091,123,539.42, default interest of RUB 408,289.76 and penalties of RUB 436,391,918.65.

437. The first-instance judgment was adopted on 3 November 2004 and upheld on appeal on 11 January 2005.

2. Tax evasion schemes involving sham rent agreements and letter-box entities registered in the domestic offshore town of Baykonur

(a) Case no. A41 K1-13539/02 (the Tax Ministry v. OAO Ufimskiy NPZ and ZAO Bort-M)

438. OAO Ufimskiy NPZ, the main production unit of one of the biggest Russian oil companies, OAO Bashneft, physically located in the town of Ufa, used the domestic tax offshore territory situated in the town of Baykonur, the territory rented by Russia from the Republic of Kazakhstan for its space-related projects. The town's tax regime was similar to that in the closed administrative-territorial formations (see above).

439. On 1 February 2001 the respondents OAO Ufimskiy NPZ and ZAO Bort-M, a letter-box entity registered in Baykonur, entered into a rent agreement whereby the entirety of OAO Ufimskiy NPZ's production facilities were rented by ZAO Bort-M in exchange for nominal compensation. Since ZAO Bort-M was registered in Baykonur, the activity of OAO Ufimskiy NPZ enjoyed lower rates in respect of excise duties. The tax authorities discovered "the scheme" and contested it in court as sham and therefore null and void.

440. On 8 October 2002 the first-instance court had regard to the substance of the transaction and, having established that, despite the contractual arrangement, OAO Ufimskiy NPZ had continued to operate the facilities in question, that furthermore the letter-box entity was never properly registered and licensed as the operator of oil processing and oil storage facilities in accordance with the relevant law, and that the letter-box entity could not operate the facility because it had rented only one part of the production cycle (which, in technological terms, could not be split in two), that the sole aim and effect of the arrangement was tax evasion and that OAO Ufimskiy NPZ and ZAO Bort-M had "malicious intent" to evade taxes, upheld the tax authorities' claim.

441. The first-instance judgment was upheld on appeal and in cassation on 17 December 2002 and 19 March 2003 respectively.

(b) Cases nos. A41 K1-13244/02 (the Tax Ministry v. OAO Novo-ufimskiy NPZ and ZAO Bort-M), A41 K1-11474/02 (the Tax Ministry v. OAO Novo-ufimskiy NPZ and OOO Korus-Baykonur), A41 K1-137828/02 (the Tax Ministry v. OAO Ufimskiy NPZ and OOO Korus-Baykonur)

442. These cases are essentially follow-ups to the previous case: OAO Novo-Ufimskiy NPZ is the second main production unit of OAO Bashneft and was involved in exactly the same tax-evasion scheme, using the sham offshore entities ZAO Bort-M and OOO Korus-Baykonur. The domestic courts examined all three cases at three instances and granted the Ministry's claims. The decisions in the first set of proceedings were taken on 9 October, 16 December 2002 and 13 March 2003. The decisions in the

second set of proceedings were taken on 19 September 2002, 5 December 2002 and 28 February 2003. The decisions in the third set of proceedings were taken on 18 December 2002, 20 February 2003 and 26 May 2003.

(c) Case no. A41 K1-9254/03 (the Tax Ministry v. OOO Orbitalnye sistemy and OAO MNPZ)

443. This case concerns exactly the same tax-evasion scheme as in the previous cases, but involves OAO MNPZ, a major oil-processing facility located in Moscow and owned by the Government of Moscow, as the defendant.

444. The decisions in the case were taken on 29 October and 27 December 2004.

(d) Case no. KA-A41/6270-03 (the Tax Ministry v. OOO Ekologiya)

445. This case also concerns the tax-evasion scheme described in the previous cases. The Ministry assessed the company, apparently a sham entity belonging to an oil producer, and found that it owed additional taxes, surcharges and penalties. The entity prevailed at first instance on 15 May 2003. On 10 October 2003 the cassation court quashed the first-instance judgment, as the lower court had failed to take into account the relevance of the entity's activity for the economy of the town of Baykonur, which was one of the criteria the law considered relevant to the issue of the lawfulness of tax exemptions.

3. Sham rent agreements and letter-box entities registered in the domestic offshore town of Ozersk (closed administrative-territorial formation, ZATO)

(a) Case no. A55-1942/04-24 (the Tax Ministry v. OAO Novokuybyshevskiy NPZ and OOO SK-STR)

446. The case concerns the same tax-evasion scheme as in the previous cases (involving the sham renting agreement), but the offshore territory at issue is the town of Ozersk and the taxpayer is OAO Novokuybyshevskiy NPZ, one of the applicant company's subsidiary oil-processing units.

447. The scheme operated from January 1999 and was prosecuted in 2004. The first-instance judgment in favour of the Ministry was taken on 13 August 2004. The court applied the same 'substance over form' approach as in the previous cases and, having assessed the defendants' conduct, the character of their relations and statements by the officials of the entities, granted the Ministry's claims and also ordered OAO Novokuybyshevskiy NPZ to pay RUB 120,688,860 in reassessed taxes.

(b) Case no. A55-5015/2004-33 (the Tax Ministry v. OAO Novokuybyshevskiy NPZ and OOO SK-STR)

448. This is a follow-up to the previous case: in the first-instance judgment the court declared the defendants' contractual arrangement to be sham and unlawful and ordered OAO Novokuybyshevskiy NPZ to pay RUB 252,963,364 in reassessed taxes.

449. The first-instance judgment in the case, dated 19 October 2004, was upheld on appeal on 19 October 2004.

(c) Case no. A55-1941/2004-40 (the Tax Ministry v. OAO Syzranskiy NPZ and OOO SK-STR)

450. This is a follow-up to the previous cases and involved OAO Syzranskiy NPZ, a production unit belonging to the applicant company. The rent agreement between the letter-box entity and the applicant company's production unit was declared sham and annulled. OAO Syzranskiy NPZ was ordered to pay RUB 30,309,119 in reassessed taxes.

451. The first-instance judgment of 18 August 2004 was upheld on appeal on 4 November 2004.

4. Sham arrangements and VAT fraud

(a) Case no. 367/96 (the Tax Ministry v. Russian-Austrian Joint Stock Enterprise "Sibservis")

452. The respondent legal entity is a privately-owned enterprise specialised in importing and assembling computer equipment. In 1995 the respondent disguised a portion of its sales as loan agreements with its clients in order to avoid payment of VAT. The first-instance judgment and the appeal decision in the case were taken on 31 August and 11 October 1995. On 17 September 1996 the Presidium of the Supreme Commercial Court of Russia reviewed the lower courts' decisions and quashed them, ordering the lower courts to investigate the exact circumstances of the case, including everything relating to "the sales disguised as loans" arrangements.

(b) Case no. A57-11990/01-5 (the Tax Ministry v. FGUP Nizhnevolzhskgeologiya)

453. The respondent legal entity is a State-owned enterprise specialising in geological exploration and identification of oil fields. In 2000 it entered into a series of deliberately unprofitable oil trading transactions with a third party, OOO Roza-Mira Processing. Since the transactions preceded the actual export of oil, the two taxpayers, acting in concert, intended to obtain an artificially increased VAT refund. Having regard to the substance of the transaction and the relevant circumstances of the case, such as the terms of actual payment and execution, the courts decided that the transactions were

sham, declared them null and void and refused the respondent's request for a VAT refund. In addition, the courts recovered the unpaid VAT with penalties.

454. The domestic courts reached their respective decisions on 22 November 2001, 29 April and 8 July 2002.

(c) Case no. 7543/02-16 (the Tax Ministry v. OAO Saratovneftegaz)

455. The respondent legal entity is the main production unit of OAO NK Russneft, a large Russian private oil company, which was involved in a dispute with the Ministry over VAT refunds in respect of its export operations. The courts established that in 2001 the respondent entered into a series of transactions with a number of third parties, aimed at deceiving the Ministry and claiming an artificially increased VAT refund. The courts took account of the overall economic effect of the transactions in their entirety, numerous discrepancies and contradictions between the contractual arrangements, the actual movement of oil, the documents certifying the customs clearance of the goods in question, etc., and refused to recognise them as valid for the purposes of reimbursement of VAT. The courts concluded that the Ministry had been acting lawfully by refusing the respondent company's request for a refund of export VAT.

456. The domestic courts reached their respective decisions on 30 June 2003, 31 May and 16 September 2004.

(d) Case no. A28-7017/02-301/21 (the Tax Ministry v. OAO Kirovskiy Shinnyy Zavod)

457. This is essentially a follow-up to the previous cases. The courts reached similar conclusions in respect of the respondent company and recovered RUB 5,000,000 in overpaid VAT in favour of the Ministry.

458. The decisions in the case during the first round of proceedings were taken on 19 December 2002, 19 March 2003 and 27 June 2003.

459. The second round of proceedings resulted in the first-instance judgment of 19 December 2002, the appeal decision of 19 March 2003 and the supervisory review decision of 23 December 2003.

(e) Case no. A09-846/03-28 (the Tax Ministry v. ZAO Melkruk, OOO Antareks-Unit, OOO Starlayt-N)

460. The first respondent legal entity is a big producer of grains, cereals and related processed products. It was involved in a dispute with the Ministry over VAT refunds in respect of export operations, whereby it had commissioned the second respondent to sell certain equipment abroad. The equipment was bought by the third respondent and resold "at an economic loss" to an entity registered in a foreign offshore location. Having regard to various circumstances, including the conduct of the entities involved and the fact that no actual hard cash had been paid for the equipment in question,

the Ministry applied to court, asking it to invalidate the transactions in question as sham. The first-instance court dismissed the claim but the appeal and cassation review courts subsequently reversed that judgment, essentially upholding the Ministry's approach.

461. The domestic courts took their respective decisions on 14 April 2003, 4 August 2003 and 10 December 2003.

(f) Case no. A09-1646/03-GK (the Tax Ministry v. OAO Belkamneft, Baxter Trading Inc, OOO Tekhnotreyd)

462. The first respondent legal entity was involved in a dispute with the Ministry over VAT refunds in respect of export operations, whereby it had entered in complex relations with the other two respondents to sell certain goods abroad. Having regard to various circumstances, including the conduct of the entities involved and the fact that no actual hard cash had been paid for the goods in question, the Ministry applied to court, asking it to invalidate the transactions in question as sham and therefore null and void. The courts at three instances upheld the Ministry's approach.

463. The domestic courts took their respective decisions on 28 December 2002, 10 April 2003 and 1 July 2003.

(g) Case no. F09-1071/03-AK (the Tax Ministry v. OOO Khudozhestvennaya masterskaya "Tvorchestvo")

464. The respondent entity was involved in a dispute with the Ministry over the latter's refusal to refund the VAT in respect of the entity's export operations. The Ministry uncovered an arrangement whereby there had been no hard cash transactions between the parties to the export operation, the respondent had "traded at a loss" and the allegedly exported produce had had nothing to do with the respondent's usual business activity. Having regard to various circumstances, including the conduct of the entities involved, the courts at three instances upheld the Ministry's approach.

465. The domestic courts took their respective decisions on 29 October 2002, 6 February 2003 and 17 April 2003.

5. Case-law of the domestic courts concerning the invalidity of sham transactions

466. By a decision dated 15 May 1997 in the case of the Tax Ministry against Commercial Bank Mechel-Bank and OAO Mechel (no. F09-162/97-AK), the Federal Commercial Court of the Ural Circuit quashed the decisions of lower courts in which they had upheld the lawfulness of a "kickback" contract which had been concluded between the respondent bank and the respondent company. The Circuit Court ruled that the lower courts had failed to study and to take account of all of the circumstances relevant to the case at issue. In particular, the court noted the finding that the contract had been concluded specifically to avoid the payment of taxes.

Accordingly, it reversed and invalidated the contract as unlawful, contrary to the legal order and morality, and ordered that the proceeds (RUB 1.5 bn) derived by the parties from the contract be seized in favour of the State.

467. In a decision of 9 December 1997 in case no. 5246/97, the Presidium of the Supreme Commercial Court of Russia invalidated a loan secured by a promissory note and a related pay-off agreement as imaginary and sham respectively. The court had regard to the terms of contracts concluded between the parties and the manner of their execution, in particular the fact that the loan had never been used by the borrower; it concluded that the transactions in question covered the sale of a promissory note and invalidated them as sham.

468. In a decision of 6 October 1998 in case no. 6202/97 the Presidium of the Supreme Commercial Court of Russia invalidated two contracts for the sale of securities and a related loan agreement as sham, having regard to the terms of contracts in question, the manner of their execution and the contractual prices. The court established that the sales contracts in fact covered the loan agreement secured by the pledge of securities and remitted the case for re-trial.

N. Enforcement proceedings in respect of a presumably solvent debtor

1. General principles

469. The Enforcement Proceedings Act (Law no. 119-FZ) of 21 July 1997 (as in force at the relevant time) establishes the procedure by which a creditor may enforce a court award against a presumably solvent legal entity debtor. According to Article 46 § 6 of the Act, execution was to be levied against the debtor's property "in such amount and such scope as is required to ensure the satisfaction of claims set out in the enforcement document".

470. Russian legislation provides for a set of special procedures in respect of presumably insolvent legal entity debtors (see section O below).

2. Term for voluntary compliance with the execution writ

471. Under section 9 (3) of the Enforcement Proceedings Act, on an application by the creditor, the bailiff institutes enforcement proceedings, fixes the time-limit for enforcement of the execution writ - which may not exceed five days from the date of institution of enforcement proceedings - and notifies the debtor accordingly.

3. Various ways to stay or delay enforcement proceedings

472. Article 324 of the Commercial Procedure Code sets out a procedure whereby a court may alter the method and order of enforcement of a final court decision. Among other thing, it provides as follows:

> "1. If there are circumstances which make it difficult to enforce the judicial act, the commercial court which issued a writ may, upon an application by the creditor, debtor or bailiff, grant respite in respect of the enforcement or arrange for the payment in instalments, or otherwise change the method or order of enforcement. ..."

473. At the same time, Articles 62, 64 (1) and (2) of the Tax Code specify that a respite or possibility of repaying in instalments concerns only the taxes, and not the interest surcharges and penalties, and may be granted by a court only for a period from one to six months from the original deadline for payment, may only be granted on specific grounds enumerated in the law and cannot be granted if there are tax proceedings pending against the applicant (Article 62 (1)).

474. The Enforcement Proceedings Act provides for three possibilities, namely: (a) to postpone enforcement actions for a term of up to 10[6] days (section 19); (b) to suspend the enforcement proceedings (section 21); or (c) to defer the execution of enforcement of a debt or arrange for payment in instalments (section 18).

475. With regard to (a), the bailiff takes the decision in the "appropriate circumstances" either on an application by the debtor or of its own motion.

476. With regard to (b), the decision may only be taken in seven enumerated cases: if the bailiff applied to the court with a request to interpret the judicial act; on a request from a debtor who has been drafted to serve in the army; if the debtor is on a long-term mission; if the debtor is hospitalised and being treated; if the actions of the bailiff are being contested in court; if the debtor himself or his property is being searched for; if the debtor or creditor are on holiday and cannot be contacted.

477. As regards (c), the debtor, creditor or bailiff has the right to request the court to defer the execution of enforcement of a debt or arrange for payment in instalments if there are "circumstances impeding the enforcement actions".

4. Seizure of the debtor's assets

478. If the debtor does not comply within the specified time-limit, under section 9 (5) of the Enforcement Proceedings Act the bailiff, on an application by the creditor, has the right to make an inventory of the debtor's property and to seize it.

479. Under section 9 (5) of the Law on Enforcement Proceedings the bailiff is empowered to seize any of the debtor's assets to secure

[6] Rectified on 17 January 2012: the text was: "up to 15 days …".

enforcement. In seizing the debtor's assets the bailiffs are obliged to follow the order of priority of arrest and sale set out in section 46 (2) of the Law on Enforcement, which provides:

> "... execution under enforcement documents shall, in the first priority, be levied on the debtor's monetary funds in roubles and in foreign currency, and on other valuables, including those kept in banks and other credit institutions".

At the same time, the Supreme Commercial Court specified in its Information Letter no. 6, dated 25 July 1996:

> "... the freezing of cash ... may not be imposed on the respondent's account and on amounts that will enter this account in the future ...".

In its Resolution no. 11 of 9 December 2002 the Plenary Supreme Commercial Court ruled:

> "... arrest on cash owned by the debtor shall be imposed not on its account in credit institutions but on cash that is on the accounts, within the limits of the monetary claims ..."

480. Section 46 (5) of the Enforcement Proceedings Act provides that, if a debtor lacks sufficient cash funds to satisfy the creditor's claims, the debt may be levied from the other forms of the debtor's property, unless the federal law states otherwise. The debtor has the right to indicate his preferred order of priority, but the final order is determined by the bailiff.

481. Section 51 of the Enforcement Proceedings Act establishes a one-month time-limit for the seizure of the debtor's property from the date on which the ruling on the institution of enforcement proceedings is served. The seizure is intended, *inter alia*, to secure the safety of the debtor's property and the creditor's claims, which shall be subject to a subsequent transfer to the creditor or to a subsequent sale. The seizure of securities is carried out in conformity with the procedure defined by the Government of the Russian Federation in Decree no. 934 "On the seizure of securities", dated 12 August 1998.

482. Section 59 of the Enforcement Proceedings Act establishes the order of priority in the seizure and forced sale of a debtor's property in three stages. Firstly, the bailiff sells property which is not immediately involved in the debtor's production cycle (securities, cash on the debtor's deposit and other accounts, currency valuables, cars, office equipment, etc.); secondly, finished products (goods) and other material values not immediately involved in production and not intended to play an immediate part in it; and, thirdly, real-estate objects, as well as raw and other materials, machine-tools and equipment and other fixed assets, intended for immediate involvement in production.

483. In Ruling no. 4 "On certain questions arising out of seizure and enforcement actions in respect of corporate shares", dated 3 March 1999, the Plenum of the Supreme Commercial Court decided that in respect of companies which had been privatised by the State as parts of bigger holding

groups through the transfer of controlling blocks of shares, the production cycle of the respective production unit should be preserved as much as possible.

5. Enforcement fee

484. Section 81 of the Enforcement Proceedings Act penalises a debtor's failure to comply voluntarily with a writ of execution with a 7% enforcement fee. Under Section 77 of the Act the fee is a priority payment which should be made by the debtor even before it begins repaying the principal debt.

485. In ruling no. 13-P of 30 July 2001 the Constitutional Court of Russia described the enforcement fee as an administrative penal sanction having a fixed monetary expression, exacted by compulsion, formalised by the decision of an authorised official and levied in favour of the State. The Constitutional Court struck the above provision down as unconstitutional, in so far as it did not allow the debtor to excuse his failure to comply with the writ by reference to certain extraordinary, objectively inevitable circumstances and to other unforeseeable and insurmountable obstacles beyond the debtor's control.

486. The Government referred to over a dozen cases from across Russia which, they claimed, confirmed that that the 7% enforcement fee was levied by bailiffs as a matter of standard practice in the event of the debtor's failure to pay, routinely and without exceptions, even if the debtor was a State-owned entity or indeed a State body. Here are some examples: enforcement proceedings dated 19 January 2001 no. 6-26/2001, in respect of RUB 304,078,000, owed by a State-owned private-law entity GUP Tatvodokanal; enforcement proceedings dated 18 November 2005 no. 3068/62/2/2006 in respect of RUB 108,083,008.64, owed by the Ministry of Education of the town of Kazan; enforcement proceedings dated 18 December 2002 no. 2-12/2002 in respect of RUB 19,0311,000, owed by OAO Tatavtodor; enforcement proceedings dated 25 February 2004 no. 7-18/04 in respect of RUB 445,336,550.84, owed by OAO Vertolety-MI; enforcement proceedings dated 13 November 2001 no. 5-17/2001 in respect of RUB 917,787,000, owed by FKP Kazanskiy zavod tochnogo mashinostroeniya imeni M. I. Kalinina.

6. Forced sale of arrested assets

(a) Rules concerning valuation of frozen property

487. Section 53 of the Enforcement Proceedings Act requires the bailiff to evaluate the arrested property on the basis of market prices on the date of execution of the enforcement writ. Should valuation be problematic for

technical or any other reasons, the bailiff is to appoint a specialist to carry out the valuation.

488. According to a Decree of the Ministry of Justice dated 27 October 1998, the bailiff is obliged to appoint a specialist to conduct the valuation if the seized property is shares or other securities (*ценные бумаги*). Under the same Decree the bailiff is to inform the debtor and creditor of the resulting valuation.

(b) General rules concerning the sale of frozen property

489. Section 54 of the Enforcement Proceedings Act requires the bailiff to sell the arrested property in satisfaction of the debt within two months of the date of seizure. The sale is carried out by a specialised institution on the basis of a commission contract with the bailiff.

490. According to Government Decree no. 418 "On the Russian Fund of Federal Property" of 29 November 2001 and Government Decree no. 260 "On the Sale of Seized, Confiscated and Other Property ..." of 19 April 2002, the Fund is entrusted with the task, *inter alia*, of auctioning property seized in satisfaction of the debts owed to Russia.

7. Distribution of levied sums and order of priority in the event of multiple claimants

491. Section 77 of the Enforcement Proceedings Act provides that, in respect of the sums levied from the debtor, including the proceeds from the forced sale of the debtor's property, the bailiffs first recover enforcement fees and all related payments and the remainder is used in satisfaction of the creditors' claims.

492. If the proceeds from the forced sale(s) are insufficient to satisfy all creditors, the following order of priority applies (section 78 of the Enforcement Proceedings Act): tort claims, employment and labour-related claims, claims made on behalf of the Pension Fund and the Social Security Fund of Russia, claims made on behalf of the budgets of various territorial levels and finally all other claims.

8. Court appeals against bailiffs' decisions

493. Under section 90 of the Enforcement Proceedings Act, all actions by the bailiff in the course of enforcement proceedings can be appealed against within ten days from the date of proper notification of the action in question.

494. Any damage inflicted on the debtor as a result of the bailiff's omission is compensated in accordance with the applicable legislation.

O. Enforcement proceedings in respect of an insolvent debtor legal entity

495. The enforcement of court awards and more generally debt claims against insolvent or presumably insolvent debtor legal entities are regulated by the Insolvency (Bankruptcy) Act of 26 October 2002 (Law no. 127-FZ).

1. Definition of the state of insolvency (bankruptcy)

496. Section 3 of the Insolvency (Bankruptcy) Act defines the state of bankruptcy of a legal entity as follows:

> "A legal entity is regarded as being unable to satisfy the claims of creditors in respect of pecuniary obligations and (or) to fulfil its obligations in respect of mandatory payments if the respective obligations and (or) obligation are not complied with within three months of the date on which compliance should have occurred."

497. In accordance with section 4 of the Act, the obligations are, as a general rule, defined/recognised by the court on the date of examination of the bankruptcy petition.

498. Bankruptcy proceedings in respect of a legal entity may only be instituted by a court if the overall amount of debt claims exceeds RUB 100,000 (section 6 of the Act).

2. Bringing of a bankruptcy petition

499. Under section 7 of the Act the debtor, the debtor's creditors in respect of pecuniary claims and State bodies competent to take part in bankruptcy proceedings in which the State is a creditor in respect of mandatory payments are entitled to bring a bankruptcy petition.

500. Whilst the executive body of the debtor has the right to file for bankruptcy in circumstances where it is obvious that the debtor would be unable to fulfil its obligation in due time (section 8 of the Act), it has a legal duty to do so if the forced seizure of the debtor's property in satisfaction of a claim would make the debtor's economic activity extremely difficult or impossible (section 9 of the Act). In this latter respect, the petition should be brought within one month from the date on which the respective relevant circumstances occurred.

501. Failure to abide by the above rules exposes the offender to civil liability action by virtue of section 10 of the Act and may also make the offender vicariously liable for any resulting damage.

3. Examination of a bankruptcy petition

502. The admissibility of the bankruptcy petition is examined by a single-judge bench (section 48 of the Act). Having declared the petition well-founded (admissible), the judge is to impose a supervision order in respect of the debtor (see below).

503. The merits of the bankruptcy petition should be examined by a court within seven months of the date of its filing (section 51 of the Act).

504. Having examined the merits of the bankruptcy petition, the court takes one of the following decisions (section 52 of the Act): (a) it declares the debtor bankrupt and applies the liquidation procedure in respect of the debtor; (b) it rejects the request to declare the debtor bankrupt; (c) it introduces a "financial improvement order" in respect of the debtor; (d) it applies the procedure of external management; (e) it discontinues the bankruptcy proceedings; (f) it disallows the bankruptcy petition; (g) it approves the friendly settlement of the case.

4. Various solutions available to a court in resolving a bankruptcy case

505. The following five procedures may be applicable in respect of the debtor in a bankruptcy case (section 27 of the Act): (a) supervision order; (b) financial improvement order; (c) external management; (d) liquidation; (e) friendly settlement.

506. A supervision order is defined as the first procedure applied to the debtor (see above). It consists of securing the debtor's property, analysing its financial condition, composing the list of creditors and carrying out the first assembly of creditors (section 2 of the Act). The decision to impose a supervision order is taken by a judge in accordance with section 9 of the Act. It can be appealed against to a higher court. In the decision, the judge should also appoint an interim receiver.

507. A financial improvement order is a bankruptcy procedure intended to re-establish the debtor's solvency and consisting in repayment of the debts in accordance with a debt repayment schedule (section 2 of the Act).

508. External management is a bankruptcy procedure intended to re-establish the debtor's solvency (section 2 of the Act).

509. Liquidation is a bankruptcy procedure applied in respect of a debtor who has been declared bankrupt. It is essentially the sale of the debtor's property by a court-appointed trustee in proportionate satisfaction of the creditors' claims (section 2 of the Act).

510. Friendly settlement is a bankruptcy procedure applicable at any stage of bankruptcy proceedings whereby the creditors and the debtor reach an agreement in respect of the debtor's liability (section 2 of the Act).

5. Supervision order and its consequences

511. The automatic consequences of the decision to adopt a supervision order in respect of the debtor legal entity (section 63 of the Act) are, in particular, the following: all debts due after the date of the decision are recoverable only pursuant to a special procedure; enforcement of execution writs already issued, including any pecuniary claims (with the exception of

those relating to payment of salaries and tort claims) against the debtor, is halted, and the seizure in respect of the debtor's property is lifted.

512. The law also introduces some restrictions in respect of operations with the debtor's shares and the actions of the debtor itself (section 64 of the Act). However, the debtor's management team remains in place, subject to limitations restricting their ability to dispose of the debtor's property above a certain value (more than 5% of the book costs of the debtor's property) or to indebt the debtor further by contracting loans, issuing guaranties or sureties, transferring debts to third parties or transferring the debtor's property for external management by a third party.

513. An interim receiver is appointed by a court in accordance with sections 45 and 65 of the Act. At this stage of proceedings, he or she has no management functions and is essentially responsible for securing the debtor's property, watching over the activities of the debtor's management, analysing the debtor's financial condition and identifying the debtor's creditors. The interim receiver is accountable to a court and is in charge of organising the first meeting of creditors.

514. For a period of thirty days from the date of publication of the supervision order notice, the creditors have the right to file their claims against the debtor (section 71 of the Act). The claims may be included in the list of creditors on the basis of the court's decision.

515. At least ten days prior to the date of termination of the supervision order, the interim receiver must organise the first meeting of creditors (section 72 of the Act). At the meeting, the creditors are competent, among other things, to decide either: (a) to introduce a financial supervision order and lodge the relevant request with the court; (b) to introduce an external management order and lodge the respective request with the court; or (c) to request the court to declare the debtor bankrupt and impose a liquidation order (section 73 of the Act).

THE LAW

I. COMPLIANCE WITH ARTICLE 35 § 2 (b) OF THE CONVENTION

516. The Court reiterates that it declared this application admissible on 29 January 2009 (see *OAO Neftyanaya Kompaniya Yukos v. Russia* (dec.), no. 14902/04, 29 January 2009) and decided to hold a hearing on the merits of the case. Subsequently, but prior to the hearing, the Court was informed that arbitration proceedings, allegedly brought against the Russian Federation by the applicant company's former owners, were pending and considered that these developments raised an issue of the applicant

company's compliance with the requirements of Article 35 § 2 (b) of the Convention. It invited the parties to address this question in their submissions at the hearing.

A. The parties' submissions

517. The Government submitted that in February 2005 the applicant company's former majority shareholders Hulley Enterprises Ltd, Yukos Universal Ltd and Veteran Petroleum Ltd, which had jointly owned over 60% of shares in the applicant company, brought arbitration proceedings against the Russian Federation for the alleged breaches of the Energy Charter Treaty in the Permanent Court of Arbitration in The Hague. The Government pointed out that the applicant company had ceased to exist and that it was obvious that the above-mentioned majority shareholders had been behind the present case in the Court and that they would be the end-beneficiaries of any eventual award in these proceedings. The Government also mentioned a number of arbitration proceedings brought against the Russian Federation by groups of minority shareholders under bilateral investment treaties. Overall, the Government invited the Court to discontinue the case with reference to Article 35 § 2 (b) of the Convention.

518. The applicant company denied any participation in and any knowledge of any other international proceedings that may be of relevance. At the same time, it invited the Court to rule that the parties in the proceedings before this Court (the applicant company) and in The Hague arbitration proceedings (the applicant company's controlling shareholders) were not the same. According to the applicant company, the subject-matter in the two cases was different. It also claimed that the arbitration proceedings in the Hague were conducted before *ad hoc* tribunals, constituted by the parties, and were not comparable to the Court in their structure, permanence or authority. Overall, the applicant company argued that its application complied with Article 35 § 2 (b) of the Convention and that any parallel proceedings should not undermine its case before the Court.

B. The Court's assessment

519. The Court will examine this issue under Article 35 § 2 (b) of the Convention, which reads as follows:

> "... 2. The Court shall not deal with any application submitted under Article 34 that ...
>
> (b) is substantially the same as a matter that has already been examined by the Court or has already been submitted to another procedure of international investigation or settlement and contains no relevant new information. ..."

520. At the outset, the Court would reiterate that Article 35 § 2 (b) of the Convention is intended to avoid the situation where several international bodies would be simultaneously dealing with applications which are substantially the same. A situation of this type would be incompatible with the spirit and the letter of the Convention, which seeks to avoid a plurality of international proceedings relating to the same cases (see, among others, *Smirnova v. Russia*, (dec.) nos. 46133/99 and 48183/99, 3 October 2002, and *Calcerrada Fornieles and Cabeza Mato v. Spain*, no. 17512/90, Commission decision of 6 July 1992, Decisions and Reports (DR) 73). In determining whether its jurisdiction is excluded by virtue of this Convention provision the Court would have to decide whether the case before it is substantially the same as a matter that has already been submitted to a parallel set of proceedings and, if that is so, whether the simultaneous proceedings may be seen as "another procedure of international investigation or settlement" within the meaning of Article 35 § 2 (b) of the Convention.

521. The assessment of similarity of the cases would usually involve the comparison of the parties in the respective proceedings, the relevant legal provisions relied on by them, the scope of their claims and the types of the redress sought (see *Vesa Peltonen v. Finland* (dec.), no. 19583/92, 20 February 1995; *Cereceda Martin and Others v. Spain*, no. 16358/90, Commission decision of 12 October 1992; *Smirnova*, cited above, and *Decision on the competence of the Court to give an advisory opinion* [GC], § 31, ECHR 2004-VI).

522. As regards the analysis of the character of parallel proceedings, the Court's examination would not be limited to a formal verification but would extend, where appropriate, to ascertaining whether the nature of the supervisory body, the procedure it follows and the effect of its decisions are such that the Court's jurisdiction is excluded by Article 35 § 2 (b) (see *Lukanov v. Bulgaria* (dec.), 21915/93, Commission decision of 12 January 1995; *Decision on the competence of the Court to give an advisory opinion* [GC], cited above; *Celniku v. Greece*, no. 21449/04, §§ 39-41, 5 July 2007, and *Peraldi v. France* (dec.), no. 2096/05, 7 April 2009).

523. Turning to the case at hand, the Court finds that there is no need for it to examine whether the proceedings in the Hague brought by the company's majority shareholders or the proceedings brought under the bilateral investment treaties brought by various groups of the company's minority shareholders may be seen as "another procedure of international investigation of settlement" as it is clear that the cases are not "substantially the same" within the meaning of Article 35 § 2 (b) of the Convention for the following reasons.

524. The Court observes that it was Hulley Enterprises Ltd and Veteran Petroleum Ltd (both registered in Cyprus) and Yukos Universal Ltd (registered in the Isle of Man), which in February 2005 initiated arbitration

proceedings against the Russian Federation before the Permanent Court of Arbitration in the Hague, referring, among other things, to the same events and proceedings as those complained of by the applicant company in the present application before the Court and alleging numerous violations of their rights as investors under the Energy Charter Treaty. Some of the company's foreign minority shareholders also initiated similar proceedings under bilateral investment treaties. The Court notes, however, that despite certain similarities in the subject-matters of the present case and of the arbitration proceedings, the claimants in those arbitration proceedings are the applicant company's shareholders acting as investors, and not the applicant company itself, which at that moment in time was still an independent legal entity.

525. The Court further notes that the present case has been introduced and maintained by the applicant company in its own name. Although the above-mentioned entities could arguably be seen as having been affected by the events leading to the applicant company's liquidation, they have never taken part, either directly or indirectly, in the Strasbourg proceedings. The Court reiterates that in November 2007 the applicant company was liquidated and that despite this fact in its admissibility decision of 29 January 2009 it nevertheless accepted the application "because the issues raised by the case transcend[ed] the person and the interests of the applicant [company]" and "... striking the application out of the list under such circumstances would undermine the very essence of the right of individual applications by legal persons, as it would encourage governments to deprive such entities of the possibility to pursue an application lodged at a time when they enjoyed legal personality...", which shows that the Court has throughout placed emphasis on the applicant company in its own right.

526. In these circumstances, the Court finds that the parties in the above-mentioned arbitration proceedings and in the present case are different and therefore the two matters are not "substantially the same" within the meaning of Article 35 § 2 (b) of the Convention. It follows that the Court is not barred, pursuant to this provision, from examining the merits of this case.

II. ALLEGED VIOLATIONS OF ARTICLE 6 OF THE CONVENTION

527. The Court notes that in the admissibility decision in this case it has established that Article 6 applied under its criminal head to the 2000 Tax Assessment proceedings and has declared admissible the company's grievances that:

(1) the Ministry had brought the action in these proceedings within the grace period;

(2) the time to prepare for trial had been too short;

(3) its lawyers could not obtain from the Ministry answers to all the questions they wished to ask in the hearings before the first-instance court and the first-instance court pronounced its judgment without having studied all the evidence;

(4) the statutory time-limit for appeal had been unjustifiably abridged;

(5) and that the appeal court had delayed the delivery of the reasons for its judgment thereby preventing the applicant company from lodging a cassation appeal.

528. The Court will examine these grievances under Article 6 of the Convention, which, in its relevant parts, provides as follows:

> "1. In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law.
>
> ...
>
> 3. Everyone charged with a criminal offence has the following minimum rights:
>
> (b) to have adequate time and facilities for the preparation of his defence; ..."

A. The parties' submissions

1. The applicant company's submissions

529. As regards the first instance proceedings, at the admissibility stage of proceedings before this Court the applicant company argued that the supporting material underlying the Tax Assessment for 2000 had first been provided to it as a result of the City Court's decision of 14 May 2004. It alleged that the disclosure did not occur until 17 May 2004, when the Ministry filed 24,000 pages of documents, and continued on 18 May 2004 with approximately 45,000 further pages and a further 2,000 pages late on 20 May 2004, i.e. on the eve of the first-instance hearing. The company conceded that its representatives had indeed been given access to all these materials, both prior to the hearings and during the trial, but submitted that the manner and time for such access had been so unsatisfactory that it was of no practical use. It also argued that it had been unable effectively to access the court's filed documents during the first-instance hearings except during the lunch breaks. Overall, the company insisted that it had had insufficient time to prepare its defence and familiarise itself with the evidence before the court and that it had not had an opportunity to take cognisance of and comment on all of the evidence adduced or observations filed, nor to express its views on every document in the file, contrary to Article 6. It referred to the *Ruiz-Mateos v. Spain* and *Krčmář v. Czech Republic* cases. In their post-admissibility observations the company

submitted that the Ministry had had sufficient time to disclose the evidence, as the relevant documents had been in the possession of the Ministry and that the Ministry could have disclosed them at any point from 8 December 2003 (some six months before the beginning of the hearing). It further noted that the documents filed by the Ministry had been in complete disorder and had been stored in nineteen plastic crates (ten of them containing six thousand pages each and nine more containing some four thousand pages each) and simply could not be studied properly over such a short period. The documents were kept in a room measuring three to four square metres and containing two chairs, a desk and one window. A request for additional space had been turned down. The above-mentioned conditions were reflected in a record dated 18 May 2004, drawn up by the applicant company's counsel. The Ministry's representative had refused to sign it and stated that he disagreed with its contents. More generally, the applicant company criticised the Ministry for bringing an action against it before the expiry of the grace period and argued that the first instance proceedings had been unfair because its lawyers could not obtain from the Ministry answers to all the questions they wished to ask in the hearings and that it was under the impression that the first-instance court had pronounced judgment without having studied all the evidence.

530. As regards the appeal proceedings, the applicant company also insisted on the breach of Article 6. It submitted that the domestic courts had failed to address the question of whether the abridgement of time had affected its substantive right to a fair hearing and that, equally, it did not rely on Article 267 of the Code of Commercial Courts Procedure, referred to by the respondent Government. Also, the rule in Article 267 requiring an appeal to be determined within one month is not respected in practice by the Russian courts; failure to comply with this requirement, even for a whole year, has no consequences for the proceedings. There was, according to the applicant company, no evidence of any particular urgency in listing or resolving the appeal: neither the Ministry, nor the co-appellant, OOO 'YUKOS' Moscow, sought expedition when their appeals were lodged and the co-appellant did not oppose the applicant company's applications to adjourn the appeal hearing. In response to the Government's criticism suggesting that the company's appeal was misaddressed by the omission of part of the postal code from the envelope, the applicant stated that no evidence had been provided of any mistake in this respect and that, after all, the appeal had been received by the court and the tax authorities. In any event, the court had made no criticism of the company in relation to the exercise of this appeal. Overall, the abridgement of the appeal period was a serious interference with the company's right to prepare for the appeal hearings, which failed to cure but rather accentuated the unfairness of the first-instance proceedings, and no substantive reason has been offered as to

why this acceleration was lawful, necessary or consistent with the requirements of a fair trial.

531. The applicant company submitted in respect of the complaint about the delay in the delivery of the appeal judgment that the delay meant that the decision had been immediately enforced against the company, rendering any further cassation appeal nugatory. Only an application for a stay of enforcement pending an appeal in cassation, coupled with a valid appeal in cassation, could have been effective against the enforcement. In the company's view, such a valid appeal was strictly dependent on filing of the reasons by the appeal court. The appeal decision had become subject to immediate forcible execution, the company had become liable for an additional surcharge of 7% of the total liability and the opportunity to exercise an effective appeal against these measures had been circumvented.

2. The Government's submissions

532. As regards the argument that the company had insufficient time for preparation of the defence, the Government referred in their admissibility observations to the domestic legislation, which established a two-month time-limit for the examination of the case at first instance (Article 134 of the Code of Commercial Courts Procedure). The applicant company had at least 37 days to prepare its defence from the date of the filing of the suit, which, in view of the above time-limit, had not been unreasonable. Furthermore, the applicant company first became aware of the Ministry's arguments on 29 December 2003, when the Ministry issued the report indicating the applicant company's large tax liability and by 12 January 2004 the company had also filed its objections to the report under Article 100 (5) of the Tax Code. Moreover, the principal arguments contained in these objections remained unchanged throughout the proceedings. It could not be said therefore that the applicant company was unprepared to state its case, since it was well aware of the Ministry's arguments five months prior to the beginning of the court proceedings. In addition, the Government pointed out that the applicant company's lawyers were given an opportunity to study the evidence both in court and at the Ministry's premises throughout May, June and July 2004. According to the documents submitted by the Government, counsel for the applicant company availed themselves of this opportunity at least on two occasions, on 18 and 19 May 2004 respectively. Lastly, the Government argued that the applicant company's arguments about insufficient time for the preparation of the case had been carefully examined and eventually dismissed by the domestic courts as unfounded. In their post-admissibility observations the Government also submitted that the proceedings before commercial courts in Russia were generally conducted without serious delays (referring, for instance, to the lack of any cases against Russia on account of length of proceedings before the commercial courts). They further argued that in its submissions the applicant company

had asserted generalities and had never mentioned any specific documents to which they had not had proper access. The evidence in question had been documents which were well known to the applicant company, as the Ministry had requested these documents from it during the on-site inspection (the Government relied on Article 101 (2) 4 of the Tax Code in this respect) and that the documents had been itemised in a register dated 17 May 2004 no. 14-3-02/22-13-1 and had been copies of original documentation reflecting the relations between the applicant company and its sham entities. In addition, the Government argued that any number of the company's lawyers could have come to study the evidence and that the applicant company had apparently felt no need to do so, since it had been represented by eight lawyers in the first-instance proceedings and only two to four of them had studied the documents. Overall, the Government suggested that the dispute was more legal rather than factual, so that the crux of the applicant company's objections concerned the interpretation of the domestic law rather than controversy about the particular circumstances of the tax evasion. In addition, the Government argued that the appeal hearing constituted a *de novo* examination of the case and that by then the applicant company had had a perfectly adequate opportunity to review the documentary record. By asking to adjourn the proceedings the applicant merely intended to delay the delivery of the judgment.

533. As regards the appeal proceedings, in the Government's view they too were in compliance with Article 6. The applicant company had brought appeal proceedings against the first-instance judgment of 26 May 2004: the possibility of review on both points of fact and law had been expressly provided for by Russian law (Article 268 of the Code of Commercial Courts Procedure) and the company had used it. Under Article 267 of the Code of Commercial Courts Procedure, which requires an appeal court to examine the appeals by the parties within a month of the date on which they were filed, the Appeal Court had to examine the case within a month of 1 June 2004, which was the date on which one party to the case, OOO 'YUKOS' Moskva, first lodged an appeal brief, notwithstanding the fact that the applicant company lodged its appeal on 17 June 2004. The appeal hearings, which represented a full re-trial of the case within the meaning of Article 268 of the Code of Commercial Courts Procedure, started on 18 June and lasted eight days, that is, until 29 June 2004, which was in line with the above rule. In addition, the applicant company deliberately delayed the examination of the case by dispatching the appeal brief to an erroneous address. Lastly, the Government underlined that the appeal decision had not been final and had been appealed against by the applicant company both in cassation instance and by way of supervisory review. The Government submitted that the fact that the reasoned copy of the Appeal Court decision of 29 June 2004 had been produced on 9 July 2004 did not affect the fairness of the proceedings as, in any event, it was open to the applicant company to lodge its cassation

appeal within a two-month time-limit from the date of delivery of the appeal decision on 29 June 2004, even in the absence of the reasoned copy of the decision. The applicant company had lodged its cassation appeal on 6 July 2004 in the absence of the reasoned copy of the appeal decision. The cassation appeal was accepted for consideration and on 17 September 2004 its full version was examined and dismissed by the Circuit Court.

B. The Court's assessment

534. The Court would reiterate that while Article 6 of the Convention guarantees the right to a fair hearing, it is not the Court's function to deal with errors of fact or of law allegedly committed by a national court and the question which must be answered is rather whether the proceedings as a whole were fair (see, for example, *Öcalan v. Turkey* [GC], no. 46221/99, §§ 148-49, ECHR 2005-IV; *Gäfgen v. Germany* [GC], no. 22978/05, §§ 162-88, ECHR 2010-...). The Court will examine the applicant company's grievances in turn to make an overall conclusion in this connection.

1. The complaint about the bringing of the action by the Ministry

535. Turning to the applicant company's complaint that in the proceedings before the Moscow City Court the action in respect of the Tax Assessment 2000 and the request to attach the company's assets as a security for the claim was brought by the Ministry within the grace period (see paragraphs 25 and 26), the Court observes that this argument was examined by the Circuit Court, which dismissed it as unfounded and recognised the Ministry's action as lawful in this respect (see paragraph 72). The Court recalls the the Ministry's action was lodged under the rule which made it unnecessary to wait until the end of the grace period if there was evidence that the dispute was insoluble and, regard being had to the circumstances of the case, finds no indication of arbitrariness or unfairness within the meaning of Article 6 of the Convention in this connection.

2. The complaint about the allegedly insufficient time for preparation of the defence at first instance

536. The Court notes that it is common ground between the parties that during the first-instance proceedings the applicant company did not have access to the documents in the court file, other than the report of 29 December 2003, the decision of 14 April 2004 and their annexes, until 17 May 2004 when the Ministry invited the company's lawyers to study the documents at its premises (see paragraphs 41-45). It is also undisputed that the hearings in the case commenced on 21 May 2004, which is four working days later, and the evidence at issue amounted to at least 43,000 pages (see paragraphs 44 and 46). It is also not in dispute that on a few occasions the

applicant company requested to adjourn the hearings referring to, among other things, their wish to study the evidence in the case, and that these requests were turned down by the trial court as unfounded (see paragraph 46).

537. The Court further notes that according to the applicant company this period was manifestly short, whilst the Government argued with reference to the sequence of the events in the proceedings and the applicant company's conduct that it had no real need to study these documents since the documents came from the company itself and it was entirely familiar with them. The Government also argued that the appeal hearing constituted a *de novo* examination of the case and that by then the applicant company had had a perfectly adequate opportunity to familiarise itself with the evidence at issue.

538. The Court reiterates that the principle of equality of arms is one feature of the wider concept of a fair trial, which also includes the fundamental right that criminal proceedings should be adversarial. The right to an adversarial trial means, in a criminal case, that both prosecution and defence must be given the opportunity to have knowledge of and comment on the observations filed and the evidence adduced by the other party. Various ways are conceivable in which national law may meet this requirement. However, whatever method is chosen, it should ensure that the other party will be aware that observations have been filed and will get a real opportunity to comment on them (see *Brandstetter v. Austria*, 28 August 1991, §§ 66 and 67, Series A no. 211; *Ruiz-Mateos v. Spain*, 23 June 1993, § 67, Series A no. 262; *mutatis mutandis*, *Milatová and Others v. the Czech Republic*, no. 61811/00, § 65, ECHR 2005-V and, *a fortiori*, *Krčmář and Others v. the Czech Republic*, no. 35376/97, §§ 41-45, 3 March 2000). Furthermore, the Court reiterates that Article 6 § 3 (b) guarantees "adequate time and facilities for the preparation of his defence" and therefore implies that the substantive defence activity on the accused's behalf may comprise everything which is "necessary" to prepare the trial. The accused must have the opportunity to organise his defence in an appropriate way and without restriction as to the possibility to put all relevant defence arguments before the trial court and thus to influence the outcome of the proceedings (see *Can v. Austria*, no. 9300/81, § 53, Commission's report of 12 July 1984, Series A no. 96, and *Moiseyev v. Russia*, no. 62936/00, § 220, 9 October 2008). The facilities which should be enjoyed by everyone charged with a criminal offence include the opportunity to acquaint himself, for the purposes of preparing his defence, with the results of investigations carried out throughout the proceedings (see *C.G.P. v. the Netherlands* (dec.), no. 29835/96, 15 January 1997, and *Galstyan v. Armenia*, no. 26986/03, § 84, 15 November 2007).

539. Turning to the case at hand, the Court observes that the Ministry's claims to the applicant company in respect of the year 2000 were based on

the audit report of 29 December 2003, which became available to the applicant company on the same date and was later used in the decision of 14 April 2004, served on the applicant on 15 April 2004. It is true that these two documents were very detailed, and contained the attachments to substantiate the Ministry's position, and that the applicant company had on a few occasions opportunity to contest them. The fact remains, however, that the object of the trial court's examination during the hearings of 21 to 26 May 2004 was neither the audit report of 29 December 2003 and the decision of 14 April 2004 as such, nor the copies of the documents allegedly already in possession of the applicant company, but rather the Ministry's court claims based on the above-mentioned two documents and the additional body of evidence filed by the Ministry and comprising at least 43,000 pages. It is clear to the Court that in order to provide the applicant company with an adversarial trial and "adequate time and facilities for the preparation of [its] defence" the applicant company should have been given an adequate opportunity to study the entirety of these documents and, more generally, to prepare for the hearings of the merits of the case on reasonable terms.

540. Having regard to the parties' arguments and the circumstances of the case, the Court is of the view that the trial court failed to reach this objective, as the mere four days during which the applicant company could have access to the case materials were insufficient for the applicant company to prepare properly, no matter the number of lawyers in its defence team or the amount of other resources which the applicant company would have been able to commit during its preparations. As regards the Government's reference to the applicant company's conduct during the proceedings and its argument that the company had no real need to study that evidence, the Court finds that it was incumbent on the trial court in the situation at hand to ensure that the applicant company had a sufficiently long period of time during which it could study such a voluminous case file and prepare for the trial hearings and it was up to the applicant company to use this time as it wished. As regards the Government's argument that the trial court was simply doing its best to comply with the two-month time-limit set out in Article 215 of the Code of Commercial Court Procedure for examination of cases of this category, the Court is of the view that even though it is no doubt important to conduct proceedings at good speed, this should not be done at the expense of the procedural rights of one of the parties, especially given the relatively short overall duration of the proceedings for a case of such magnitude and complexity.

541. Overall, the Court is of the view that the applicant company did not have sufficient time to study the case file before the first instance hearings.

542. The Court takes note of the Government's argument that any possible defects in the fairness of the proceedings at first instance have been remedied on appeal or in the cassation instance. Since this argument is too

closely related to the applicant company's complaint about the early beginning of the appeal hearings in the 2000 Tax Assessment case, the Court will examine them together below.

3. The complaints about the trial hearings and the allegedly bad quality of the first instance judgment

543. As regards the applicant company's allegations that its lawyers could not obtain answers from the Ministry to all the questions they wished to ask in the hearings before the court and that the trial court abruptly interrupted the pleadings of the applicant company's lawyer, the Court finds that these complaints are vague and unspecific and there is nothing in the company's arguments to suggest that the conduct restrictions imposed by the first-instance or appeal court on the company's counsel during the hearings were arbitrary or adversely affected the fairness of the proceedings as a whole. The Court also finds unsubstantiated the applicant company's allegation that the Moscow City Court had given its judgment without having studied the evidence.

4. The complaints about the early beginning of the appeal hearings

544. The Court observes that under Articles 257 and 259 of the Code of Commercial Court Procedure a party has thirty days to file its appeal (see paragraph 422 above). It further notes that the full text of the first-instance judgment of 26 May 2004 became available to the parties on 28 May 2004 and that, despite the applicant company's requests for adjournment, the appeal hearing in the case commenced on 18 and lasted until 29 June 2004 (see paragraphs 51, 57 and 58).

545. The Court finds that the beginning of the appeal proceedings on 18 June 2004, that is, twenty-one days after the full text of the first-instance judgment on 28 May 2004 had become available, restricted the applicant company's ability to advance its arguments and, more generally, to prepare for the appeal hearings by shortening the statutory time-limit by nine days. Given the number of the participants, the complexity and magnitude of the case as well as the previous restrictions on the applicant company's ability to study the case at first instance, the Court finds that the applicant company did not have "adequate time and facilities for the preparation of [its] defence" within the meaning of Article 6 § 3 (b) on account of the restricted time for preparation of the appeal hearing. It also finds that the appeal court failed to acknowledge, let alone to remedy the shortcomings committed by the first-instance court as regards the applicant company's restricted access to the case file.

546. In so far as the Government relied on Article 267 of the Code of Commercial Court Procedure to justify the promptness in question, the Court would again reiterate that the legitimate goal of conducting proceedings at

good speed should not have been achieved at the expense of the procedural rights of one of the parties, especially given the lack of any indication of unjustified delays in the proceedings which lasted at the first two instances for only 3 months and 15 days. In any event, the Court is not persuaded by the interpretation of the text of the provision in question suggested by the Government. It would take note of the fact that recently the domestic authorities themselves have found it necessary to modify and explain the provision in question by amending it (see paragraphs 422 and 423). In its present day version the time-limit in question lasts two months rather than one, and starts running only after the expiry of the time-limit for bringing appeals, and not simultaneously to it, as suggested by the Government in its submissions. In addition, the appeal court now has the discretion to increase the term up to six months, depending on the number of the participants and the complexity of the case.

547. Lastly, in so far as the respondent Government argued that the subsequent examination of the case at the cassation instance had remedied these shortcomings, the Court observes that the cassation hearing took place on 17 September 2004, four months after the disclosure of the evidence and about three months after the appeal hearing which took place between 18 and 29 June 2004. Despite the fact that the company may have had enough time to prepare for the cassation hearing, the cassation court, as a review court, had restricted competence in relation to the assessment of evidence already made by the first-instance and appeal courts (see paragraph 426) and, on the facts, it failed to recognize any shortcomings in the judgments of the lower courts (see paragraph 71).

548. Overall, the Court finds that the early beginning of the appeal hearing impeded the applicant company's ability to prepare and present properly its case on appeal.

5. The complaint about the alleged delay in the production of a reasoned version of the appeal judgment

549. In so far as the applicant company also complained about the alleged delay in providing the reasons for the Appeal Court's judgment in the proceedings in respect of the 2000 Tax Assessment, the Court would note that the applicant company did not complain about the proceedings in cassation as such but rather claimed that, in its situation, effective access to the cassation court was impossible without a stay of enforcement of the appeal decision of 29 June 2004. In this respect, the Court observes that the immediate enforcement of the appeal decision did not prevent the company from lodging its cassation appeal and whilst Article 6 provides an applicant with the right of access to court, it does not guarantee, as such, the right to an automatic stay of enforcement of an unfavourable court decision. The Court would underline that the applicant company in the present case had access to courts of two levels of jurisdiction before any enforcement

measures were taken and that the enforcement of the appeal decision of 29 June 2004 did not make it impossible for the applicant company to exercise its right to appeal in cassation, or to pursue further proceedings by way of supervisory review or before the Constitutional Court. The applicant company lodged its cassation appeal and additional submissions on the basis of the reasoned copy of the appeal decision of 29 June 2004 on 7 July 2004 (see paragraph 67). The appeal was accepted for consideration, and on 17 September 2004 its full version was examined and dismissed by the Circuit Court (see paragraph 70). Not only the cassation appeal, but also the request to stay the enforcement of the appeal decision of 29 June 2004 were examined by the domestic courts at two instances and eventually dismissed as unfounded (see paragraphs 127-129).

550. Overall, the Court concludes that there is no indication of unfairness within the meaning of Article 6 on account of the alleged restrictions on the applicant company's access to the cassation instance.

6. Conclusion

551. Having regard to the above, the Court finds that the applicant company's trial did not comply with the procedural requirements of Article 6 of the Convention for the following reasons: the applicant company did not have sufficient time to study the case file at first instance, and the early beginning of the hearings by the appeal court unjustifiably restricted the company's ability to present its case on appeal. The Court finds that the overall effect of these difficulties, taken as a whole, so restricted the rights of the defence that the principle of a fair trial, as set out in Article 6, was contravened. There has therefore been a violation of Article 6 § 1 of the Convention, taken in conjunction with Article 6 § 3 (b).

III. ALLEGED VIOLATIONS OF ARTICLE 1 OF PROTOCOL No. 1, TAKEN ALONE AND IN CONJUNCTION WITH ARTICLES 1, 7, 13, 14 AND 18 OF THE CONVENTION

552. Under Article 1 of Protocol No. 1, taken alone and in conjunction with Articles 1, 7, 13, 14 and 18 of the Convention, the applicant company complained about the allegedly unlawful, arbitrary and disproportionate imposition and enforcement of the 2000-2003 Tax Assessments. The company complained furthermore that the sale of OAO Yuganskneftegaz had been unlawful, arbitrary and disproportionate.

553. These grievances fall to be examined principally under Article 1 of Protocol No. 1, regard being had, where appropriate, to other Convention provisions relied on by the applicant company.

Article 1 of Protocol No. 1 reads:

"Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.

The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties."

554. The Court reiterates that in accordance with its constant and well-established case-law Article 1 of Protocol No. 1 comprises three distinct rules. The first rule, which is of a general nature, enounces the principle of peaceful enjoyment of property; it is set out in the first sentence of the first paragraph. The second rule covers deprivation of possessions and subjects it to certain conditions; it appears in the second sentence of the same paragraph. The third rule recognises that the States are entitled, amongst other things, to control the use of property in accordance with the general interest, by enforcing such laws as they deem necessary for the purpose; it is contained in the second paragraph. The three rules are not, however, "distinct" in the sense of being unconnected. The second and third rules are concerned with particular instances of interference with the right to peaceful enjoyment of property and should therefore be construed in the light of the general principle enunciated in the first rule (see *Sporrong and Lönnroth v. Sweden*, 23 September 1982, § 61, Series A no. 52, and *James and Others v. the United Kingdom*, 21 February 1986, § 37, Series A no. 98).

555. The Court notes that between December 2003 and January 2005 the domestic authorities subjected the applicant company to a number of measures in connection with its alleged failure to pay the correct amount of tax for the years 2000-2003. In particular, as a result of the Tax Assessment proceedings the applicant company was found guilty of repeated tax fraud and was ordered to pay an overall sum of at least RUB 572 billion (around EUR 16 billion) in outstanding taxes, default interest and penalties. In the enforcement proceedings, simultaneously conducted, the applicant company was ordered to pay an additional 7% enforcement fee on the overall amount of the debt: its assets were attached and seized, whilst 76.79 percent of shares in its main production unit, OAO Yuganskneftegaz, were sold in satisfaction on the mentioned liability.

556. The Court notes that the parties did not dispute that these measures, whether taken alone or together, constituted an interference with the applicant company's property rights as guaranteed by Article 1 of Protocol No. 1. The Court further notes that the company complained about the measures separately and that it also complained about the Government's intentions in connection with those measures. In this latter respect, the applicant company argued that, in bringing the relevant proceedings, the

authorities had sought to destroy the company and expropriate its assets. The Court has now to satisfy itself that each instance of such interference met the requirement of lawfulness, pursued a legitimate aim and was proportionate to the aim pursued.

557. Having regard to the circumstances of the case and the nature of the applicant company's complaints, the Court finds that the complaints concerning the separate decisions and measures in the context of the proceedings against the applicant company fall to be examined under the third rule of Article 1 of Protocol No. 1, taken in conjunction, where appropriate, with other Convention provisions relied on by the applicant company. The Court will examine the complaints in the following order:

(A) the complaints about various aspects of the tax assessment proceedings for the years 2000-2003;

(B) the complaints concerning the measures taken by the domestic authorities to enforce the debt resulting from the tax assessment proceedings on the applicant company and the Government's related plea of non-exhaustion, which in the decision on admissibility of 29 January 2009 it joined to the merits;

(C) the applicant company's allegations concerning the Government's intentions in these proceedings, made under Article 18 of the Convention, taken in conjunction with Article 1 of Protocol No. 1.

A. The complaints about the Tax Assessments 2000-2003

558. The Court reiterates that it was not in dispute between the parties that the Tax Assessments 2000-2003 represented an interference with the applicant company's property rights. It remains to be determined whether these decisions met the requirement of lawfulness, pursued a legitimate aim, were proportionate to the aim pursued, as required by Article 1 of Protocol No. 1, and whether they were not discriminatory within the meaning of Article 14 of the Convention, taken in conjunction with Article 1 of Protocol No. 1.

1. Compliance with Article 1 of Protocol No. 1

(a) Whether the Tax Assessments 2000-2003 complied with the Convention requirement of lawfulness

559. The Court reiterates that the first and most important requirement of Article 1 of Protocol No. 1 is that any interference by a public authority with the peaceful enjoyment of possessions should be lawful: the second paragraph recognises that the States have the right to control the use of property by enforcing "laws" (see *Iatridis v. Greece* [GC], no. 31107/96, § 58, ECHR 1999-II). This means that the interference should be in compliance with the domestic law and that the law itself be of sufficient

quality to enable an applicant to foresee the consequence of his or her conduct. As regards the compliance with the domestic law, the Court has limited power in this respect since it is a matter which primarily lies within the competence of the domestic courts (see *Håkansson and Sturesson v. Sweden*, 21 February 1990, § 47, Series A no. 171-A, and, *mutatis mutandis*, *Tre Traktörer AB v. Sweden*, 7 July 1989, § 58, Series A no. 159). As regards the quality of the law, the Court's task is to verify whether the applicable provisions of domestic law were sufficiently accessible, precise and foreseeable (see *Hentrich v. France*, 22 September 1994, § 42, Series A no. 296-A, and *Lithgow and Others v. the United Kingdom*, 8 July 1986, § 42, Series A no. 110). In so far as the tax sphere is concerned, the Court's well-established position is that States may be afforded some degree of additional deference and latitude in the exercise of their fiscal functions under the lawfulness test (see *National & Provincial Building Society, Leeds Permanent Building Society and Yorkshire Building Society v. the United Kingdom*, 23 October 1997, §§ 75-83, *Reports* 1997-VII) and that, in view of the complexity of the relevant field of regulation, corporate entities, as opposed to individual taxpayers, may be required to act with additional caution and diligence by consulting competent specialists in this sphere (see *Špaček, s.r.o., v. the Czech Republic*, no. 26449/95, § 59, 9 November 1999).

560. The applicant company argued in respect of the Tax Assessment 2000 that prosecution for tax evasion had been time-barred. Furthermore, it also argued that the decisions in question had been generally unlawful in that they had not been based on any reasonable and foreseeable interpretation of the domestic law, for which reason there had been no basis in law to impose taxes, double fines or to deny the repayment of VAT in respect of the export of oil and oil products. The applicant company also complained that it had been the first entity ever to have been punished for the tax optimisation scheme, hitherto generally tolerated.

i. The allegation that the prosecution for the alleged tax evasion during the year 2000 was time-barred

α. The applicant company's submissions

561. The applicant company complained that in the Tax Assessment proceedings for the year 2000 the domestic courts had failed to apply the three-year statutory time-bar set out in Article 113 of the Tax Code. Since the relevant claims by the Ministry had been time-barred by virtue of Article 113 of the Tax Code, the Tax Assessment 2000 had been unlawful, unforeseeable and retroactive in the light of the decision of the Constitutional Court of 14 July 2005. It also noted that this domestic provision applied to tax assessments proceedings in general and not just to

fines and that the doubling of the fines for the year 2001 had also been unlawful.

β. The Government's submissions

562. The Government disagreed. They underlined that the issue only concerned the fines for the year 2000, and not reassessed taxes or surcharges. They argued that the decision of the Constitutional Court of 14 July 2005 had simply confirmed the proper application of Article 113 of the Tax Code for all taxpayers, that it explained the meaning of this norm, that this meaning had been in line with international practice and that it had not been aimed at the applicant individually. The Government also stated that the decision had concerned the specific situation of a bad-faith tax evasion where a taxpayer hinders and obstructs tax inspections, and also relied on examples from foreign jurisdictions, where specific rules apply to taxpayers in such situations. They quoted certain Russian cases where the courts applied the Constitutional Court's ruling in a manner similar to that in the applicant company's case and also referred to the Court's judgment in the case of National & Provincial Building Society, Leeds Permanent Building Society and Yorkshire Building Society v. the UK. They also noted that the three-year time-limit had not been particularly long and that in other countries time-limits were even longer.

γ. The Court's assessment

563. The Court finds at the outset that this grievance concerns the outcome of the Tax Assessment proceedings for the year 2000 only in the part concerning the imposition of penalties, since Article 113 of the Tax Code which provided for the time-limit in question, only applied to the collection of fines (see paragraph 403) and that no similar Convention issues arise in respect of the collection of additional taxes and interest payments (see paragraph 404). The Court further notes that Article 113 of the Tax Code provided for a three year time-limit for holding a taxpayer liable and that this period ran from the first day after the end of the relevant tax term. According to the practice directions of the Supreme Commercial[7] Court dated 28 February 2001, the moment at which a taxpayer was held liable within the meaning of Article 113 of the Tax Code was the date of the relevant decision of the tax authority (see paragraph 405 and 406).

564. On the facts, such a decision in connection with the company's activities in the year 2000 was adopted on 14 April 2004 (see paragraph 21), which was clearly outside the above-mentioned three year time-limit. In response to the argument raised by the applicant company during the court proceedings, the lower courts decided that the rules on a statutory time-bar were inapplicable because the applicant company had been acting in bad

[7] Rectified on 17 January 2012: "Commercial" was added.

faith (see paragraph 49). Thereafter the supervisory review instance decided that such an interpretation of the rules on the statutory time-limits had not been in line with the existing legislation and case-law (see paragraph 80) and referred the issue to the Presidium of the Supreme Commercial Court, which, in turn, referred it to the Constitutional Court (see paragraph 81).

565. Having initially refused to consider the applicant company's individual complaint concerning the same issue (see paragraphs 76 and 77), the Constitutional Court accepted the reference from the Presidium of the Supreme Commercial Court and on 14 July 2005 gave a decision in which it disagreed with the lower courts (see paragraphs 82-88), noting that the rules on the limitation period should apply in any event and that, exceptionally, if a taxpayer impeded the inspections by the tax authorities, and thereby delayed the adoption of the relevant decision, the running of the time-limit could be suspended by the adoption of a tax audit report setting out the circumstances of the tax offence in question and referring to the relevant articles of the Tax Code. Thereafter the case was referred back to the Presidium of the Supreme Commercial Court which applied this interpretation to conclude that the applicant company had been actively impeding the tax inspections (see paragraphs 17 and 90). Since the audit report in respect of the year 2000 had been adopted and served on 29 December 2003, the court decided that the Ministry's claims for 2000 had been brought on time. The Court notes that the Constitutional Court's decision of 14 July 2005 resulted in a change in the interpretation of the relevant rules on the statutory time-limits of the proceedings. Accordingly, an issue arises as to whether such a change was compatible with the requirement of lawfulness of Article 1 of Protocol No. 1.

566. In making its assessment the Court will take into account its previous finding that the 2000 Tax Assessment proceedings were criminal in character (see *OAO Neftyanaya kompaniya Yukos* (dec.), cited above, § 453) and will also bear in mind that the change in question concerned the collection of fines for intentional evasion of tax. In this connection, it would again reiterate that the third rule of this Convention provision explicitly reserves the right of Contracting States to pass "such laws as they may deem necessary to secure the payment of taxes" which means that the States are afforded an exceptionally wide margin of appreciation in this sphere (see *Tre Traktörer AB v. Sweden*, 7 July 1989, §§ 56-63, Series A no. 159).

567. The Court reiterates the principle, contained primarily in Article 7 of the Convention but also implicitly in the notion of the rule of law and the requirement of lawfulness of Article 1 of Protocol No. 1, that only law can define a crime and prescribe a penalty. While it prohibits, in particular, extending the scope of existing offences to acts which previously were not criminal offences, it also lays down the principle that the criminal law must not be extensively construed to an accused's detriment, for instance by analogy. It follows that offences and the relevant penalties must be clearly

defined by law. This requirement is satisfied where the individual can know from the wording of the relevant provision and, if need be, with appropriate legal assistance, what acts and omissions will make him criminally liable (see *Coëme and Others v. Belgium*, nos. 32492/96, 32547/96, 32548/96, 33209/96 and 33210/96, §§ 145-146, ECHR).

568. Furthermore, the term "law" implies qualitative requirements, including those of accessibility and foreseeability (see, among other authorities, *Cantoni v. France*, 15 November 1996, § 29, *Reports of Judgments and Decisions* 1996-V; and *E.K. v. Turkey*, no. 28496/95, § 51, 7 February 2002). These qualitative requirements must be satisfied as regards both the definition of an offence and the penalty the offence in question carries (see *Achour v. France* [GC], no. 67335/01, § 41, ECHR 2006-IV). The Court has acknowledged in its case-law that however clearly drafted a legal provision may be, in any system of law, including criminal law, there is an inevitable element of judicial interpretation. There will always be a need for elucidation of doubtful points and for adaptation to changing circumstances. Again, whilst certainty is highly desirable, it may bring in its train excessive rigidity and the law must be able to keep pace with changing circumstances. Accordingly, many laws are inevitably couched in terms which, to a greater or lesser extent, are vague and whose interpretation and application are questions of practice (see, *mutatis mutandis*, *Sunday Times v. the United Kingdom (no. 1)*, 26 April 1979, § 49, Series A no. 30 and *Kokkinakis v. Greece*, 25 May 1993, § 40, Series A no. 260-A). The role of adjudication vested in the courts is precisely to dissipate such interpretational doubts as remain (see *Cantoni*, cited above, § 29).

569. Thus, the requirement of lawfulness cannot be read as outlawing the gradual clarification of the rules of criminal liability through judicial interpretation from case to case, "provided that the resultant development is consistent with the essence of the offence and could reasonably be foreseen" (see *Kafkaris v. Cyprus* [GC], no. 21906/04, § 141, ECHR 2008-...).

570. The Court previously defined limitation as the statutory right of an offender not to be prosecuted or tried after the lapse of a certain period of time since the offence was committed. Limitation periods, which are a common feature of the domestic legal systems of the Contracting States, serve several purposes, which include ensuring legal certainty and finality and preventing infringements of the rights of defendants, which might be impaired if courts were required to decide on the basis of evidence which might have become incomplete because of the passage of time (see *Stubbings and Others v. the United Kingdom*, 22 October 1996, § 51, *Reports* 1996-IV).

571. Turning to the facts of the case, the Court would note firstly that the rule which, in the present case, underwent changes as a result of the decision of 14 July 2005, was contained in Article 113 of Chapter 15

"General provisions concerning the liability for tax offences" of the Tax Code (see paragraph 403) and thus formed a part of the domestic substantive law. Even though the rule in itself did not describe the substantive elements of the offence and the applicable penalty, it nevertheless constituted a *sine qua non* condition with which the authorities had to comply in order to be able to prosecute the relevant taxpayers in connection with the alleged tax offences. Accordingly, Article 113 of the Tax Code defined a crime for the purposes of the Court's analysis of lawfulness. It remains to be determined whether in the circumstances the decision of 14 July 2005 could be seen as a gradual clarification of the rules on criminal liability which "[was] consistent with the essence of the offence and could reasonably be foreseen" (see *Kafkaris*, cited above, § 141).

572. In this connection the Court may accept that the change in question did not change the substance of the offence. The Constitutional Court interpreted the existing rules on time-limits in relation to taxpayers who acted abusively. At the same time, the Court is not persuaded that the change in question could have been reasonably foreseen.

573. It observes that the decision of 14 July 2005 had changed the rules applicable at the relevant time by creating an exception from a rule which had had no previous exceptions (see paragraphs 86 and 88). The decision represented a reversal and departure from the well-established practice directions of the Supreme Commercial Court (see, by contrast, *Achour*, cited above, § 52) and the Court finds no indication in the cases submitted by the parties suggesting a divergent practice or any previous difficulty in connection with the application of Article 113 of the Tax Code at the domestic level (see paragraphs 407-408). Although the previous jurisprudence of the Constitutional Court contained some general references to unfavourable legal consequences which taxpayers acting in bad faith could face in certain situations, these indications, as such, were insufficient to provide a clear guidance to the applicant company in the circumstances of the present case.

574. Overall, notwithstanding the State's margin of appreciation in this sphere, the Court finds that there has been a violation of Article 1 of Protocol No. 1 on account of the change in interpretation of the rules on the statutory time-bar resulting from the Constitutional Court's decision of 14 July 2005 and the effect of this decision on the outcome of the Tax Assessment 2000 proceedings.

575. Since the applicant company's conviction under Article 122 of the Tax Code in the 2000 Tax Assessment proceedings laid the basis for finding the applicant company liable for a repeated offence with a 100% increase in the amount of the penalties due in the 2001 Tax Assessment proceedings, the Court also finds that the 2001 Tax Assessment in the part ordering the applicant company to pay the double fines was not in accordance with the law, as required by Article 1 of Protocol No. 1.

ii. The allegation that the Tax Assessments 2000-2003 had not been based on a reasonable and foreseeable interpretation of the domestic law

α. The applicant company's submissions

576. The applicant company disagreed with the factual conclusions reached by the domestic courts in respect of the trading companies. In its submission on the admissibility of the case, the applicant company argued that it had been the wrong defendant in the tax assessment proceedings, that there had been no links of dependency between the trading companies and itself, and that there were no grounds for making the applicant company, a holding company with, at the material time, only two employees with highly important but small-scale administrative functions, liable for the trading companies' tax liabilities and creating a previously virtually unknown concept of "bad-faith taxpayer". In its submissions on the merits of the case, the applicant company argued that "the Yukos Group", including the trading companies, had operated as a unit and that the authorities had been aware of all the details of this unit's functioning, including its relations with the trading companies, because all the entities forming the group made regular tax declarations. The company also submitted that the Ministry made regular checks of the whole group, involving the mapping of the entire course of every link in the chain of transactions from the original purchase of oil by the trading companies until its export, and that Yukos officials held monthly meetings with the Ministry's officials to discuss the company's functioning and tax returns. Overall, the applicant company considered that its tax arrangement had never been secret.

577. The applicant company also submitted that Russian law had contained no legal provision allowing for the attribution of tax liabilities as had occurred in its case, that the denial of VAT reductions had been unlawful, that the use of domestic off-shores by the applicant company had been lawful, that the legal theories used by the authorities in its case had been without legal precedent, that the way in which the authorities had assessed taxes had led to double taxation, and that the payment of interest and fines had been domestically unlawful. As regards the attribution of tax liabilities, the applicant company considered that Russian law contained no provisions that permitted piercing of the corporate veil in order to hold one company liable for the actions of another, whether the latter was a subsidiary, an affiliate or a separate entity. The company claimed that the legal theories used by the Ministry in its tax assessment cases had been unprecedented and it referred to legal remedies that could have been used by the Ministry in this situation but had not been employed. In particular, the applicant company argued that the authorities should have applied the anti-transfer pricing mechanism of Articles 20 and 40 of the Tax Code or that the courts should have invalidated individual transactions by the trading companies so as to make either them or the applicant company's

subsidiaries liable for the allegedly underpaid tax. The applicant company considered that in any event, under the applicable domestic law, the authorities could not have held it directly liable for the actions of the trading companies. Furthermore, the company relied on Article 251 (1) 11 of the Tax Code to justify the unilateral transfers of cash from the trading companies to the applicant company's Fund. It argued that there had been no such notion as "sham entity" in Russian law and that the "bad faith" doctrine had been too vague a legal tool to be used to prosecute it. The applicant company also submitted to the Court an opinion dated 7 September 2003 by the company's counsel, the law firm "Pepelyev, Goltsblat i Partnery", confirming the lawfulness of the arrangement whereby "a subsidiary company makes a transfer of its profits to the parent company, which in turn creates a Fund [out of these monies] to return them to the subsidiary companies for use ... or to pay the dividends" and also relied on case no A42-6604/00-15-818/01 to demonstrate that its tax arrangement had been lawful at domestic level. Lastly, the applicant company considered that the Government's explanations in this connection and in particular its reference to Articles 168, 169 and 170 of the Civil Code could not justify the authorities' actions in the tax assessment proceedings, since these provisions had not been relied upon by the domestic courts.

578. The applicant company further argued that the denial of tax benefits to the trading companies and the failure to repay VAT in respect of the export of oil and oil products had been unlawful and unsubstantiated. The applicant argued that the Ministry had known about all of the trading companies' transactions because of their monthly VAT returns and regular requests for tax refunds, and that since all of the traded oil had been for export and exempt from VAT its use of tax arrangements with the trading companies had not achieved any savings in this connection. Both in its initial application to the Court and in further submissions on the admissibility of the case, the applicant company expressed dissatisfaction with the domestic courts' refusal to recalculate the amount of the VAT due in the relevant Tax Assessment proceedings, purportedly as a result of the company's failure to file for VAT refunds in its own name. In its final submissions to the Court at the hearing on 4 March 2010, the company alleged that on 31 August 2004 it had filed the VAT exemption forms in its own name for each of the years 2000 to 2003. In addition, with reference to Article 75 (3) of the Tax Code, the applicant company claimed that it should not have been ordered to pay interest surcharges at all.

β. The Government's submissions

579. In their admissibility observations the Government stated that the tax inspections in respect of the applicant company had been conducted in accordance with the domestic law and that the company had been acting in bad faith throughout the proceedings, in blatant breach of tax legislation,

and had merely been mimicking compliance with the law. In respect of the factual conclusions of the domestic courts, they argued that the applicant company had committed blatant tax evasion, as confirmed by the findings of the domestic courts. The evidence to confirm the Ministry's claims was abundant and it was clear that the whole setup with trading companies was organised solely for the purpose of tax evasion. During the proceedings the applicant company had been unable to explain the economic reasons for the transactions in question. As an example of the sham nature of the arrangement, the Government referred to the fact, established by the domestic courts in the proceedings against the applicant company, that on one occasion a person managing one of the company's sham entities signed three contracts simultaneously in three different locations, namely Samara, Nefteyugansk and the Tomsk region, situated at great distances from each other. In addition, the Government referred to an "internal" opinion by the audit company PriceWaterhouseCoopers, which specifically mentioned various problems with the applicant company's "tax optimisation" scheme, including the Fund used by the company for receiving the money generated by the sham entities, and mentioned by the Appeal Court in its decision of 29 June 2004. This was in breach of the Russian legislation, as money could only be transferred from one independent commercial entity to another independent commercial entity in exchange or payment for services or goods (Article 575 of the Civil Code). In addition, the company misled the public in its reports and financial statements. For example, in February 2004 in its report for nine months of the year 2003 under the US Generally Accepted Accounting Principles standards, the company accounted for the difference between the nominal profit tax rate and the actual rate by its use of affiliate companies registered in foreign tax havens. This statement was not true since, as established by the domestic courts, the applicant company used sham entities located in domestic tax havens. The widespread use of promissory notes was also mentioned by the auditor as being non-compliant with the legislation in force. The Government submitted that the company's management had used this opportunity to present a distorted picture of the company's performance and thus attract investors.

580. As regards the lawfulness of the company's use of domestic tax havens, the Government referred to statements by a senior partner in the law firm "Pepelyaev, Goltsblat i Partnery", which advised the applicant company and its majority shareholder, Group Menatep. In an interview with the Raschyot magazine of 30 January 2001, he stated that, as time passed, any widely replicated optimisation scheme became known to the tax authorities and they started fighting it. Penalties were being imposed with regard to low quality schemes, but the better quality schemes remained safe. The use of Russian low-tax regions was a crude form: where a company was registered in, for example, Kalmykiya, while the director, office and bank account were in Moscow. In such instances the court would rule that

the location of the organisation was Moscow and not Kalmykiya. The scheme would be ruined and the company be forced to pay in Moscow. However, there could be more subtle schemes, where everything was arranged in such a way that the director, accountant and some staff were in Kalmykiya and there was an account in a Kalmyk bank, [and] thus the organisation would appear to have an actual presence there. Certainly, business would be conducted in Moscow but through another company, so that the entire profit went through appropriate contracts to Kalmykiya. Such subtle schemes were left untouched because formally there was nothing to pick on. According to the Government, the applicant company used the schemes described in their crudest form and undoubtedly knew that such schemes were illegal.

581. In respect of the lawfulness of the domestic authorities' actions, the Government submitted that the company's tax liability had been established by the domestic courts on the basis of, among other things, Article 122 of the Tax Code, which penalised the understatement of revenues and corresponding taxes, RF Law no. 2116-1 of 27 December 1991 "On profit tax of enterprises and organisations", RF Law no. 1759-I of 18 October 1991 "On road funds in the Russian Federation", RF Law no. 2118-I of 27 December 1991 "On the basics of the tax system", RF Law no. 2030-I of 13 December 1991 "On property tax of enterprises", RF Law no. 1992-I of 6 December 1991 "On valued-added tax" and RF Law no. 3297-I of 14 July 1992 "On closed administrative territorial entities", which were all clear and foreseeable at the relevant time.

582. In their post-admissibility observations, the Government submitted that the company's tax arrangement, consisting of the systemic use of dozens of shell entities which were controlled by the applicant company, organised in special low-tax zones within Russia, transfers of profits from the shell entities to the applicant company and multiple layers of trading activities between the company's production units and the ultimate customer, had been clearly unlawful and had one and only one aim – to avoid payment of taxes. The applicant company tried to hide its involvement in this scheme by renaming the shell entities on a regular basis and by operating through a complex system of promissory notes' exchanges aimed at hiding the transfers of profits from the shell entities to the company. The whole setup had been managed by the applicant company, although on paper the shell entities had been owned and managed by third parties.

583. The Government also described instances where the applicant company had actively resisted the authorities by failing to present the necessary tax documents following requests by the Ministry, by attempting to hide its corporate register just prior to its seizure by the bailiffs, by making multiple offers of payment with shares in OAO Sibneft (which in reality had not belonged to the applicant company), by lying about its

financial status and by rejecting the Ministry's tax claims in respect of years 2001 to 2003 instead of cooperating.

584. As regards the lawfulness of the manner in which the authorities had assessed the applicant company's liability for additional taxes, the Government relied on the Constitutional Court's judgment no. 14-P dated 28 October 1999, which had endorsed the 'substance-over-form' approach, and to the extensive case-law of the commercial courts in interpreting and applying it. In all of these cases, exactly the same method as that used by the authorities in the applicant company's case had been used – i.e. the courts had looked behind appearances and taken account of the substance of the transactions in question. As regards the bad-faith theory, the Government relied on two decisions of the Constitutional Court, nos. 138-O and 168-O, dated 25 July 2001 and 8 April 2004 respectively, and the case-law of the commercial courts. They also relied on international experience, quoting rules adopting the substance over form approach in the UK, France, Germany, Italy and the US.

585. As regards the VAT repayments, the Government insisted that the domestic law clearly adopted an approach whereby the owner of the goods in question should apply for any VAT reductions and relied on judgment no. 12-P of the Constitutional Court, dated 14 July 2003, and the extensive case-law of the commercial courts to substantiate their point. They also referred to rules in the UK and France to show that these countries used essentially the same approach in respect of VAT refunds. More generally, the Government also argued that the refusal to grant VAT repayment was a direct consequence of the company's own recklessness in operating its tax optimisation plans and that it had failed to make any attempts to comply with the legal requirements for VAT refunds even after the tax fraud had been exposed. The Government submitted that the applicant company had never made any applications for VAT refunds in its own name.

586. The Government also stated that all of the cases cited in their observations had been available in the legal database Konsultant-Plus. The authorities could not be accused of having tolerated the company's tax optimisation, as they could not have had any prior knowledge of it on account of its complex and well-masked character. They also argued that the present case had a moral and social dimension, in the sense that the applicant company had been one of the biggest taxpayers in Russia, that many social programmes run by the State had depended on the company's tax payments, that the company's resources had been transferred to it during privatisation in exchange for their efficient and honest use, and that the colossal scope of the tax evasion had led to an incorrect redistribution of wealth and the denial of their social responsibility by a small number of the company's core shareholders. The Government also insisted that the Court take into account the wide margin of appreciation which is mentioned in the Convention and recognised by the Convention case-law in any assessment

of the company's complaints. They disagreed with the applicant company's argument regarding expropriation, as the Government viewed the events referred to by the applicant company as a mere enforcement of tax laws. In addition, they drew the Court's attention to the fact that the applicant company had consistently presented incomplete or untrue information in their arguments.

587. Lastly, they again referred to the statements on tax optimisation techniques made in 2001 by a senior partner in a law firm advising the applicant company and its controlling shareholder, in which, in the Government's opinion, he had openly conceded that the company's techniques had been unlawful and that everything depended on whether or not the given arrangements would be discovered by the authorities. In the Government's view, if this adviser knew this, then his clients, the company's majority shareholders, could not have failed to be aware of the unlawfulness of the arrangement and any associated risk.

γ. The Court's assessment

588. The Court notes that in this complaint the applicant company challenged the lawfulness of the Tax Assessments 2000-2003 only in the part linked to the payment of reassessed taxes. The examination will therefore be confined to the question of the lawfulness of the additional tax liability. The Court further notes that the company did not seem to dispute that the relevant laws made it clear what taxes were due, at what rate and when. Rather, the company claimed that in 2000, 2001, 2002 and 2003 it used lawful "tax optimisation techniques" which were only subsequently condemned by the domestic courts in 2004, 2005 and 2006. It also complained that any existing legal basis for finding the company liable fell short of the Convention requirements in respect of the quality of the law and that, in any event, the application of the relevant laws contradicted established practice. Accordingly, the Court has to determine whether the relevant tax arrangements were domestically lawful at the time when the relevant transactions took place and whether the legal basis for finding the applicant company liable was sufficiently accessible, precise and foreseeable.

589. Turning to the first question, the Court would note at the outset that the applicant company disputed the findings of the domestic courts concerning the nature of relations between the applicant company and its trading entities. In view of its conclusion that the tax assessment proceedings in respect of the year 2000 did not comply with the requirements of Article 6 §§ 1 and 3 (b) of the Convention, the Court is required to decide whether the factual assessments made by the domestic courts could be used for the purposes of its legal analysis under Article 1 of Protocol No. 1. In this respect, the Court reiterates that according to its well-established case-law it is not its task to take the place of the domestic courts,

which are in the best position to assess the evidence before them and establish the facts. The Court will not, in principle, intervene, unless the decisions reached by the domestic courts appear arbitrary or manifestly unreasonable (see, *mutatis mutandis*, *Ravnsborg v. Sweden*, 23 March 1994, § 33, Series A no. 283-B; *Bulut v. Austria*, 22 February 1996, § 29, *Reports of Judgments and Decisions* 1996-II, and *Tejedor García v. Spain*, 16 December 1997, § 31, *Reports* 1997-VIII) or if the court decisions have been issued in "flagrant denial of justice" (compare *Stoichkov v. Bulgaria*, no. 9808/02, § 54, 24 March 2005).

590. Having examined the materials of the case and the parties' submissions and despite its earlier conclusions under Article 6 §§ 1 and 3 (b) of the Convention in respect of the 2000 Tax Assessment (see paragraph 551), the Court has little doubt that the factual conclusions of the domestic courts in the Tax Assessment proceedings 2000-2003 were sound. The factual issues in all of these proceedings were substantially similar and the relevant case files contained abundant witness statements and documentary evidence to support the connections between the applicant company and its trading companies and to prove the sham nature of the latter entities (see paragraphs 14-18, 48, 62-63, 165, 191-193, 212 and 213). The applicant company itself did not give any plausible alternative interpretation of this rather unambiguous evidence, as examined and accepted by the domestic courts.

591. From the findings of the domestic courts and the parties' explanations, the Court notes that the company's "tax optimisation techniques" applied with slight variations throughout 2000-2003 consisted of switching the tax burden from the applicant company and its production and service units to letter-box companies in domestic tax havens in Russia. These companies, with no assets, employees or operations of their own, were nominally owned and managed by third parties, although in reality they were set up and run by the applicant company itself. In essence, the applicant company's oil-producing subsidiaries sold the extracted oil to the letter-box companies at a fraction of the market price. The letter-box companies, acting in cascade, then sold the oil either abroad, this time at market price or to the applicant company's refineries and subsequently re-bought it at a reduced price and re-sold it at the market price. Thus, the letter-box companies accumulated most of the applicant company's profits. Since they were registered in domestic low-tax areas, they enabled the applicant company to pay substantially lower taxes in respect of these profits. Subsequently, the letter-box companies transferred the accumulated profits unilaterally to the applicant company as gifts. The Court observes that substantial tax reductions were only possible through the mixed use and simultaneous application of at least two different techniques. The applicant company used the method of transfer pricing, which consisted of selling the goods from its production division to its marketing companies at

intentionally lowered prices and the use of sham entities registered in the domestic regions with low taxation levels and nominally owned and run by third persons (see paragraphs 14-18, 48, 62-63 for a more detailed description).

592. The domestic courts found that such an arrangement was at face value clearly unlawful domestically, as it involved the fraudulent registration of trading entities by the applicant company in the name of third persons and its corresponding failure to declare to the tax authorities its true relation to these companies (see paragraphs 311, 349-353, 374-380). This being so, the Court cannot accept the applicant company's argument that the letter-box entities had been entitled to the tax exemptions in questions. For the same reason, the Court dismisses the applicant company's argument that all the constituent members of the Yukos group had made regular tax declarations and had applied regularly for tax refunds and that the authorities were thus aware of the functioning of the arrangement. The tax authorities may have had access to scattered pieces of information about the functioning of separate parts of the arrangement, located across the country, but, given the scale and fraudulent character of the arrangement, they certainly could not have been aware of the arrangement in its entirety on the sole basis on the tax declarations and requests for tax refunds made by the trading companies, the applicant company and its subsidiaries.

593. The arrangement was obviously aimed at evading the general requirements of the Tax Code, which expected taxpayers to trade at market prices (see paragraphs 395-399), and by its nature involved certain operations, such as unilateral gifts between the trading companies and the applicant company through its subsidiaries, which were incompatible with the rules governing the relations between independent legal entities (see paragraph 376). In this connection, the Court finds relevant the warning given by the company's auditor about the implications of the use of the company's special fund during the year 2002 (see paragraphs 206-209) and is not persuaded by the applicant company's reference to case no. A42-6604/00-15-818/01 (see paragraphs 356-357), the expert opinion of its counsel (see paragraph 577) and its reliance on Article 251 (1) 11 of the Tax Code (see paragraph 376).

594. By contrast to the Tax Assessments in issue, the respondent entity in case no. A42-6604/00-15-818/01 was not alleged to have been part of a larger tax fraud and the Ministry failed to prove that it had been sham. The courts established that the entity had some assets, employees and a bank account at the place of its registration and dismissed the Ministry's claims. As regards the expert opinion and the company's reference to Article 251 (1) 11 of the Tax Code, the Court finds them irrelevant as they refer to the relations of openly associated companies and not, as was the case at issue, to the use of sham entities fraudulently registered in the name of certain third parties. Thus, the Court cannot agree with the applicant

company's allegation that its particular way of "optimising tax" had been previously examined by the domestic courts and upheld as valid or that it had used lawful "tax optimisation techniques" which were only subsequently condemned by the domestic courts. The above considerations are sufficient for the Court to conclude that the findings of the domestic courts that applicant company's tax arrangements were unlawful at the time when the company had used them, were neither arbitrary nor manifestly unreasonable.

595. The Court will now turn to the question whether the legal basis for finding the applicant company liable was sufficiently accessible, precise and foreseeable. In this connection, the Court notes that in all the Tax Assessments (see paragraphs 14-18, 48, 62-63, 165, 191-193, 212 and 213) the domestic courts essentially reasoned as follows. The courts established that the trading companies had been sham and had been entirely controlled by the applicant company and accordingly reclassified the transactions conducted by the sham entities as transactions conducted in reality by the applicant company.

596. The courts first decided that the transactions of the sham entities failed to meet the requirements of Article 39 of the Tax Code defining the notion of a sales operation (see paragraphs 48 and 324) as well as Article 209 of the Civil Code describing essential characteristics of an owner of goods (see paragraph 48 and 381). In view of the above and relying on Article 10 (3) of the Civil Code which established a refutable presumption of good faith and reasonableness of actions of the parties in commercial transactions (see paragraph 48 and 382-383), the courts then changed the characterisation of the sales operations of the sham entities. They decided that these were in reality conducted by the applicant company and that it had been incumbent on the latter to fulfil the corresponding obligation to pay various taxes on these activities. Finally, the courts noted that the setting up and running of the sham arrangement by the applicant company resulted in an understating of the taxable base of its operations and, as a consequence, the intentional non-payment of various taxes, which was punishable as a tax offence under Article 122 of the Tax Code (see paragraph 400).

597. Having regard to the applicable domestic law, the Court finds that, contrary to the applicant company's assertions, it is clear that under the then rules contractual arrangements made by the parties in commercial transactions were only valid in so far as the parties were acting in good faith and that the tax authorities had broad powers in verifying the character of the parties' conduct and contesting the legal characterisation of such arrangements before the courts. This was made clear not only by Article 10 (3) of the Civil Code relied on by the domestic courts in the Tax Assessment proceedings, but also by other relevant and applicable statutory provisions which were available to the applicant company and other

taxpayers at the time. Thus, Article 45 (2) 3 of the Tax Code explicitly provided the domestic courts with the power to change the legal characterisation of transactions and also the legal characterisation of the status and activity of the taxpayer, whilst section 7 of the Law on the Tax Authorities of the Russian Federation granted the right to contest such transactions to the tax authorities (see paragraph 393). In addition, the case-law referred to by the Government indicated that the power to re-characterise or to cancel bad faith activities of companies existed and had been used by the domestic courts in diverse contexts and with varying consequences for the parties concerned since as early as 1997 (see paragraphs 382-393 and paragraphs 428-468). Moreover, in a number of its rulings, including decision of 25 July 2001 no. 138-0 specifically relied upon by the domestic courts in the Tax Assessment proceedings against the applicant company (see paragraphs 384-387), the Constitutional Court confirmed the significance of this principle, having mentioned various possible consequences of a taxpayer's bad faith conduct.

598. In so far as the applicant company complained that the bad faith doctrine had been too vague, the Court would again reiterate that in any system of law, including criminal law, there is an inevitable element of judicial interpretation and there will always be a need for elucidation of doubtful points and for adaptation to changing circumstances. In order to avoid excessive rigidity, many laws are inevitably couched in terms which, to a greater or lesser extent, are vague and whose interpretation and application are questions of practice (see, among other authorities, *Sunday Times*, cited above, § 49 and *Kokkinakis*, cited above, § 40). On the facts, it would be impossible to expect from a statutory provision to describe in detail all possible ways in which a given taxpayer could abuse a legal system and defraud the tax authorities. At the same time, the applicable legal norms made it quite clear that, if uncovered, a taxpayer faced the risk of tax reassessment of its actual economic activity in the light of the relevant findings of the competent authorities. And this is precisely what happened to the applicant company in the case at hand.

599. Overall, having regard to the margin of appreciation enjoyed by the State in this sphere and the fact that the applicant company was a large business holding which at the relevant time could have been expected to have recourse to professional auditors and consultants (see *Špaček, s.r.o.*, cited above, § 59), the Court finds that there existed a sufficiently clear legal basis for finding the applicant company liable in the Tax Assessments 2000-2003.

600. Lastly, the Court observes that the applicant company made a number of additional arguments under this head. In particular, it also alleged that there was no basis in law to deny the repayment of VAT in respect of the export of oil and oil products, that the domestic courts had failed to apply Articles 20 and 40 of the Tax Code, that it should have been

dispensed from payment of interest surcharges under Article 75 (3) of the Tax Code and that in respect of the year 2000 the company had been subjected to double taxation in respect of the profits of the sham entities.

601. The Court notes that both Section 5 of Law no. 1992-1 of 6 December 1991 "On Value-Added Tax" governing the relevant sphere until 1 January 2001 as well as Article 165 of the Tax Code applicable to the subsequent period provided unequivocally that a zero rate of value-added tax in respect of exported goods and its refund could by no means be applied automatically, and that the company was required to claim the tax exemptions or refunds under its own name under the procedure set out initially in Letter no. B3-8-05/848, 04-03-08 of the State Tax Service of Russia and the Ministry of Finance and subsequently in Article 176 of the Tax Code to substantiate the requests in order to obtain the impugned refunds (see paragraphs 326-336). In view of the above, the Court finds that the relevant rules made the procedure for VAT refunds sufficiently clear and accessible for the applicant company to able to comply with it.

602. Having examined the case file materials and the parties' submissions, including the company's allegation made at the hearing on 4 March 2010 that it had filed the VAT exemption forms for each of the years 2000 to 2003 on 31 August 2004, the Court finds that the applicant company failed to submit any proof that it had made a properly substantiated filing in accordance with the established procedure, and not simply raised it as one of the arguments in the Tax Assessment proceedings, and that it had then contested any refusal by the tax authorities before the competent domestic courts (see paragraphs 49 and 171, 196, 196 and 216). The Court concludes that the applicant company did not receive any adverse treatment in this respect.

603. As regards the company's argument that Articles 20 and 40 of the Tax Code should have been applied by the domestic courts in their case and that the Ministry's claims were inconsistent with the above provisions, the Court notes that the Ministry and the domestic courts never relied on these provisions and there is nothing in the applicable domestic law to suggest that they had been under a legal obligation to apply these provisions to the applicant company's case. Thus, it cannot be said that the authorities' failure to rely on these provisions rendered the Tax Assessments 2000-2001 unlawful.

604. Finally and in so far as the company disagreed with the interpretation of Article 75 (3) of the Tax Code by the domestic courts and also alleged to have been subjected to double taxation, the Court would again reiterate that it is not its task to take the place of the domestic courts, which are in the best position to assess the evidence before them, establish the facts and to interpret the domestic law. On the facts, the former provision only applied to cases where the taxpayer was unable to pay the tax debt solely due to the seizure of its assets and cash funds (see paragraph 402).

The domestic courts established that the company had been unable to pay because of the lack of funds and not because of the injunctions and refused to apply Article 75 (3) of the Tax Code in the applicant's case (see paragraph 216). The Court does not find this conclusion arbitrary or unreasonable. Likewise, the Court finds nothing in the parties' submissions or the case file materials to cast doubt on the findings of the domestic courts, which specifically established that the Ministry took account of the sham entities' profits in calculating their claims so as to avoid double taxation (see paragraph 49).

605. Overall, the Court finds that, in so far as the applicant company's argument about the allegedly unreasonable and unforeseeable interpretation of the domestic law in the Tax Assessments 2000-2003 is concerned, the Tax Assessments 2000-2003 complied with the requirement of lawfulness of Article 1 of Protocol No. 1.

(b) Whether the Tax Assessments 2000-2003 pursued a legitimate aim and were proportionate

606. The Court is satisfied that, subject to its findings in respect of the lawfulness of fines for the years 2000 and 2001 made earlier, each of the Tax Assessments 2000-2003 pursued a legitimate aim of securing the payment of taxes and constituted a proportionate measure in pursuance of this aim. The tax rates as such were not particularly high and given the gravity of the applicant company's actions there is nothing in the case file to suggest that the rates of the fines or interest payments can be viewed as having imposed an individual and disproportionate burden, as such, on the applicant company (see *Dukmedjian v. France*, no. 60495/00, §§ 55-59, 31 January 2006).

(c) Conclusion concerning the compliance with Article 1 of Protocol No. 1 as regards the Tax Assessments 2000-2003

607. Overall, the Court finds that there has been a violation of Article 1 of Protocol No. 1 on account of the 2000-2001 Tax Assessments in the part relating to the imposition and calculation of penalties. Furthermore, the Court finds that there has been no violation of Article 1 of Protocol No. 1 as regards the rest of the 2000-2003 Tax Assessments.

2. Compliance with Article 14, taken in conjunction with Article 1 of Protocol No. 1

(a) The applicant company's submissions

608. The applicant company argued that the courts' interpretation of the relevant laws had been selective and unique, since many other Russian companies such as Sibneft and TNK International Ltd. had also used domestic tax havens.

609. The company also submitted that the authorities had tolerated and even endorsed the tax optimisation techniques used by the applicant company in that they had accepted the applicant company's and its trading companies' tax returns and payments on a regular basis, and the company's rate of tax payment had been comparable to or even higher than that of its competitors. In this connection, the applicant company relied on statistical data contained in a report by the Centre for Development, a report of the Financial Research Institute and reports of the Accounts Chamber of Russia. The company also under this heading argued that the legislative framework had permitted the company to use such techniques and that the interpretation of the domestic law in its case had been unique, selective and unforeseeable.

(b) The Government's submissions

610. The Government responded that the allegations that other taxpayers may have used similar schemes could not be interpreted as justifying the applicant company's failure to abide by the law. They further contended that the occurrence of illegal tax schemes at a certain stage of Russia's historical development was not due to failures or drawbacks in the legislation, but rather due to "bad-faith" actions by economic actors and weakened governmental control over compliance with the Russian tax legislation on account of objective criteria, such as the 1998 economic crisis and the difficulties of the transition period.

611. At present, the Government was constantly combating tax evasion and strengthening its control in this sphere. They also referred to statistical data by AK&M and some other news agencies in 2002, which had reported that OAO LUKOIL and OAO Surgutneftegas, two other large Russian oil producers, had posted sales proceeds of RUB 434.92 billion and RUB 163.652 billion and paid RUB 21.190 billion and RUB 13.885 billion in profit tax respectively, whilst the applicant company had posted sales proceeds of RUB 295.729 billion and paid only RUB 3.193 billion in profit tax. The Government submitted that at least two Russian oil majors, OAO Surgutneftegaz and OAO Rosneft, had never engaged in such practices, whilst some, in particular OAO Lukoil, had ceased using them in 2002.

(c) The Court's assessment

612. The Court will examine this grievance under Article 14 of the Convention, taken in conjunction with Article 1 of Protocol No. 1. This former provision reads:

Article 14 of the Convention

"The enjoyment of the rights and freedoms set forth in [the] Convention shall be secured without discrimination on any ground such as sex, race, colour, language,

religion, political or other opinion, national or social origin, association with a national minority, property, birth or other status."

613. Before considering the complaints made by the applicant company, the Court would reiterate that Article 14 does not forbid every difference in treatment in the exercise of the rights and freedoms recognised by the Convention (see, for example, *Lithgow and Others*, cited above, § 117). It safeguards persons (including legal persons) who are "placed in analogous situations" against discriminatory differences of treatment; and, for the purposes of Article 14, a difference of treatment is discriminatory if it "has no objective and reasonable justification", that is, if it does not pursue a "legitimate aim" or if there is not a "reasonable relationship of proportionality between the means employed and the aim sought to be realised" (see, amongst many authorities, *Rasmussen v. Denmark*, 28 November 1984, §§ 35 and 38, Series A no. 87). Furthermore, the Contracting States enjoy a certain margin of appreciation in assessing whether and to what extent differences in otherwise similar situations justify a different treatment in law; the scope of this margin will vary according to the circumstances, the subject-matter and its background (*ibid.*, § 40).

614. The Court would reiterate that nothing in the case file suggests that the applicant company's tax arrangements during the years 2000-2003, taken in their entirety, including the use of fraudulently registered trading companies, were known to the tax authorities or the domestic courts and that they had previously upheld them as lawful (see paragraphs 592-594). It thus cannot be said that the authorities passively tolerated or actively endorsed them.

615. As regards the applicant company's allegation that other domestic taxpayers used or continue to use exactly the same or similar tax arrangements as the applicant company and that the applicant company was the only one to have been singled out, the Court finds that the applicant company failed to demonstrate that any other companies were in a relevantly similar position. The Court notes that the applicant company was found to have employed a tax arrangement of considerable complexity, involving, among other things, the fraudulent use of trading companies registered in domestic tax havens. This was not simply the use of domestic tax havens, which, depending on the exact details of an arrangement, may have been legal or may have had some other legal consequences for the companies allegedly using them. The Court notes that the applicant company had failed to submit any specific and reliable evidence concerning such details. It further notes that it cannot be called upon to speculate on the merits of the tax arrangements of third parties on the basis of data contained in non-binding research and information reports and that therefore it cannot be said that the situation of these third parties was relevantly similar to the situation of the applicant company in this respect.

616. The Court concludes that, in so far as the complaint about discriminatory treatment is concerned, there has been no violation of Article 14 of the Convention, taken in conjunction with Article 1 of Protocol No. 1.

B. The complaints about the enforcement of the debt resulting from the Tax Assessments 2000-2003

617. The Court now has to determine whether the manner in which the domestic authorities enforced the debt resulting from the 2000-2003 Tax Assessment proceedings on the applicant company complied with the requirements of Article 1 of Protocol No. 1.

618. The Court reiterates that the enforcement of the debt resulting from the Tax Assessments 2000-2003 involved the seizure of the company's assets, the imposition of a 7% enforcement fee on the overall amount of the debt and the forced sale of the applicant company's main production unit OAO Yuganskneftegaz. These measures constituted an interference with the applicant company's rights under Article 1 of Protocol No. 1 and it remains to be decided whether these measures met the requirement of lawfulness, pursued a legitimate aim and were proportionate to the aim pursued.

1. The applicant company's submissions

619. The applicant company complained that the enforcement proceedings in its case had been unlawful, disproportionate and arbitrary. In particular, it argued that the authorities ought to have allowed the company to settle the debt and that it had been wrong to sell off its main production unit at auction with such speed. The company complained that the courts ought to have intervened and corrected the assessment of this matter by the bailiffs. The authorities should have first considered and accepted its offers of shares in OAO Sibneft, and/or allowed the company to make deferred payments over a prolonged period. As regards such deferred payments, the company submitted that the domestic law and practice gave priority to such a solution and that OAO Rosneft was able to obtain such a deferral in respect of the tax debts of OAO Yuganskneftegaz following the auction of 19 December 2004. The company argued that it could have repaid the debt, entirely or in part, had it not been for the attachment imposed by the court. It further criticised the authorities' failure to act during the twenty-two months following the auctioning of OAO Yuganskneftegaz, as well as the imposition of an unlawful and disproportionate enforcement fee.

620. The applicant company contended that the seizure had been disproportionate in that the authorities had ordered the applicant company to pay and, at the same time, had frozen the company's assets, which were worth considerably more than the company's then liability. The authorities refused to use the company's equity in the Sibneft company or other realistic means of settling the debt. According to the applicant company, the

domestic authorities should have accepted those other realistic means of settlement (letter of 5 July 2004, letter of 9 August 2004, letter of 4 November 2004, letter of 23 March 2006) because they were required to do so by precedent in the practice of the commercial courts. The period of merely a couple of days granted to the applicant company for payment was absurdly short.

621. The applicant company was also of the view that the sale of OAO Yuganskneftegaz had been unlawful, disproportionate and had resulted in gross undervaluing by means of a clearly controlled auction with the unlawful participation of a sham bidder, OOO Baykalfinansgrup. It disagreed with the decision to sell OAO Yuganskneftegaz, arguing that under the domestic legislation OAO Yuganskneftegaz should have been the last item to be auctioned, and that the auction had been incapable of generating a reasonably good price because of the limited number of candidates, the widespread perception of the need for political support to acquire the item in question and insufficient time for preparation. The applicant company was also dissatisfied with the decision to sell only the voting shares of OAO Yuganskneftegaz, as opposed to all of the shares. The company argued that even though the authorities put no open obstacles in the path of potential buyers, there had been practical obstacles, such as the need for the buyers to comply with internal corporate procedures and to request anti-competition clearance.

622. More generally, the applicant company viewed the auction as a sham, because OAO Gazprom, OAO Rosneft (both State-owned companies with considerable involvement of State officials in their day-to-day management), the organisers of the auction and the bailiffs were acting in concert. It also relied on interviews by the then President of Russia and argued that the State banks had financed the acquisition and that the State had failed to apply anti-monopoly laws in connection with the auction. The company argued that its actions in the US bankruptcy court had had no effect on the outcome of the auction of OAO Yuganskneftegaz because neither OAO Rosneft nor OOO Baykalfinansgrup had applied for participation before the company filed for bankruptcy in the U.S.

623. The applicant company argued that the above circumstances showed that the proceedings against it, taken as a whole, were abusive in that the State clearly wanted to destroy the company and to take control of its assets.

624. As regards its alleged failure to exhaust domestic remedies, the applicant company considered that exhaustion had been unnecessary in view of the lack of prospects of success. The domestic courts consistently rejected the company's attempts to contest the actions of the bailiffs, so other attempts would have been futile. In any event, the company had not contested the valuation report in respect of OAO Yuganskneftegaz, since it was not so materially inaccurate as to be realistically challenged in

litigation. Furthermore, the company submitted that it did challenge the entire process by which the voting shares in OAO Yuganskneftegaz were sold to a state-owned company, OAO Rosneft.

2. The Government's submissions

625. The Government submitted that the enforcement proceedings in respect of the applicant company had been lawful and proportionate.

626. It argued that the company had failed properly to exhaust domestic remedies in respect of this part of the application. In particular, its complaints about the seizure of property pending the enforcement proceedings, the alleged failure of the bailiffs to grant the company access to the case in the enforcement proceedings, the alleged inaction of the bailiffs in respect of the Sibneft's shares, the order to pay a 7% enforcement fee and the circumstances of valuation and sale of OAO Yuganskneftegaz were inadmissible on account of a failure to exhaust domestic remedies.

627. The Government pointed out that, in the course of the enforcement proceedings, there had been no restrictions on the company's production cycle or the sale of petroleum and mineral oils and that the applicant company had remained fully operational. In view of the State's wide margin of appreciation in the fiscal sphere and the applicant company's abusive conduct, illustrated by its attempts to hinder enforcement action by hiding the register of the shareholders of its three largest subsidiary companies, the Government were of the view that the fair balance between the private and public interests had been struck.

628. The Government further submitted that the procedure for compulsory recovery of arrears of mandatory tax payments had been used in respect of the applicant company, that such tax payments were recovered by way of charging the company's cash flows on bank accounts, that in the case of insufficient or non-existent funds, the recovery of tax was carried out using the taxpayer's assets and that the whole procedure was described in detail in the domestic legislation and had been followed by the authorities. In the circumstances, the measures represented the control of the use of property and were in full compliance with the Convention.

629. As regards the seizure of property, the Government referred to the *Gasus Dosier* and *AGOSI* cases and considered that, having regard to relevant factors, such as the enormous amount of arrears, the bad-faith conduct of the applicant company and the need for an expedient and efficient recovery of tax to the State budget, the measure in question was in compliance with the requirements of Article 1 of Protocol No. 1. The Government submitted that both the seizure and freezing orders were usual practice, both domestically and internationally, and their use was especially appropriate in the present case because of the unprecedented amounts of the tax debts, the unrepentant and defiant attitude of the applicant company, claims that the authorities' actions were a "malicious tax racket" and the

applicant company's history, namely its management and core shareholders moving corporate assets into new shell entities and sometimes into foreign tax havens. These measures were merely precautionary in character.

630. In respect of the April injunction, the Government disagreed with the applicant company's claim that it could have repaid the debt but for the seizure of its assets. The injunction did not cover either cash or cash revenues and the applicant company did subsequently repay a portion of its debt using the cash in the frozen account. The applicant company could have had the injunction lifted had it provided adequate counter-security, which it failed to do, or liquidated some of its foreign assets not covered by the injunction. The Government maintained that instead of selling its foreign assets to meet its tax debts the applicant company simply stripped them away, which in itself proved that the company's complaint about the injunction was unsubstantiated. As regards the freezing orders, the Government submitted that they had been issued by the bailiffs pursuant to court writs dated 30 June 2004, which froze the company's accounts in Russian banks as of the date of issue of the respective freezing orders. The company could still dispose of cash added to its frozen accounts after 30 June 2004 and could use its non-seized accounts abroad. The funds in these accounts had been far lower than the company's then liabilities. The Government further noted that as of 14 July 2004 the applicant company had still to pay 96.5% of its then liability and that the company's voluntary payment only commenced on 14 July 2004, apparently as a response to the seizure of the shares of OAO Yuganskneftegaz. The very fact that the payments had been made through the frozen accounts demonstrated that the company's allegations about the effects of the cash freezing orders were untrue.

631. As regards the proposals for respite and payment spread, the applicant company first made such a request on 16 July 2004 by sending a letter to the Ministry of Finance. The Government pointed out that the Ministry of Finance had not been the proper authority to grant these measures as only a commercial court could and that the law set out clear rules regarding the conditions that should have been satisfied so that the request could be granted, i.e. the request should have been made one to six months before the original payment deadline and on specific grounds only, such as the risk of bankruptcy. In addition, the law did not allow for respite and payment spread if there were pending tax proceedings against the taxpayer at issue. The applicant not only failed to substantiate its request with reference to the criteria set out in law, but it was also clear that such a request was bound to fail because of the pending tax proceedings against the applicant company.

632. The Government relied on the applicable domestic law and cases to demonstrate that asking a guilty taxpayer to pay within one or two days had been standard and lawful practice followed in all cases. They claimed that

this period was sufficient, as taxpayers usually learned about tax claims - with a specific indication of the sums to be paid - in the Ministry's audit reports, which were usually served from several weeks to a few months in advance. Thus, in the present case the applicant company had first learned of the Ministry's claims for the years 2000-2003 109, 66, 19 and 18 days in advance. More generally, in such cases the taxpayer usually knew well in advance the sums that had been underpaid (typically during tax evasion), so it cannot claim that it was unprepared. In addition, very similar practices existed internationally.

633. As to the choice of OAO Yuganskneftegaz as the first item to be auctioned in satisfaction of the company's liabilities, the Government pointed out that the offers made by the applicant company had been unacceptable. The first three offers, made on 22 April, 2 July and 13-14 July 2004, all involved various portions of shares of OAO Sibneft, allegedly owned by the applicant company. All three offers were rejected, not only because the company's ownership of these shares had been contested in various unrelated proceedings by third persons, but also because the offers had been made in violation of injunctions issued by the courts in the above-mentioned unrelated proceedings. In fact, the sale of shares that did belong to the applicant company (some 20%) would have been insufficient to cover the company's then debt, even in part, let alone satisfy the Ministry's upcoming claims for the years 2001-2003. It was a minority stake of uncertain value and any such value was in any event insufficient to satisfy the company's tax arrears. As regards the fourth offer, dated 9 August 2004, it involved 20% of OAO Sibneft and a farrago of shares in fifteen companies (some of them subsidiaries, some of them minority stakes and all of uncertain liquidity). In any event, this offer was "too little and too late" for the Government, since preparation for the auctioning of OAO Yuganskneftegaz had been under way. The above-mentioned "shopping list" did not offer any guarantee of a "good chance of fetching a price sufficient to discharge much of [the applicant's] rapidly increasing tax liabilities" and in addition involved a high risk of third-party claims to the property in question in each case.

634. The Government maintained that the choice of OAO Yuganskneftegaz was lawful under Russian law, aimed at securing the payment of taxes and had been effected in full compliance with the provisions of the Federal Enforcement Proceedings Act. Under section 54 (2) of the Enforcement Proceedings Act, the sale of the applicant company's property was made by a specialised organisation pursuant to the terms of commission and the relevant legislation. On 18 November 2004 the bailiffs decided to sell 43 shares (76.8%) of OAO Yuganskneftegaz at auction. The Government noted that OAO Yuganskneftegaz was itself the debtor in mandatory payments to the budget totalling RUB 102.09 billion, so that the above arrears inevitably affected the price of the auctioned shares, as defined by the

valuation institution and the results of the auction. The date of the auction and invitation to participate in the open auction were published in the mass media in due time. The auction itself was open, both with regard to its participants and to the form of submissions of price bids. Bids were received between 19 November and 18 December 2004. On 19 December 2004 the open auction took place. The winner of the auction was recognised as OOO Baykalfinancegrup, which offered RUB 260,753,447,303.18 for the shares in question. The auction itself was public. The mass media representatives provided extensive media coverage. The results were published in the mass media and broadcast. With regard to the proportionality of the sale, the sum of 260.5 billion roubles generated as a result of the sale did not, however, cover the arrears of OAO Yukos entirely. The Government also underlined that the subsequent bankruptcy was not caused by the sale of OAO Yuganskneftegaz, but had been initiated by a consortium of foreign banks and that the representatives of the applicant company had allegedly acknowledged that the company had been in good financial condition even despite the sale of OAO Yuganksneftegaz. In sum, the Government considered that there had been no breach of the Convention.

3. The Court's assessment

635. The applicant company submitted a number of grievances about these proceedings. In particular, the applicant company complained that the enforcement of the tax liability had been deliberately orchestrated with a view to preventing the applicant company from repaying its debts. In this connection the company maintained that the seizure of its assets pending litigation had prevented it from repaying the debt. It was furthermore dissatisfied that it had been ordered to pay a 7% enforcement fee in respect of the entirety of its debt, that the time for voluntary compliance with the Tax Assessments 2000-2003 had been too short and that the sale of the company's main production unit OAO Yuganskneftegaz had been unlawful, arbitrary and generally disproportionate.

636. Before turning to the substance of these complaints, the Court reiterates that in its decision on admissibility it joined to the merits the question of exhaustion of domestic remedies. Thus, the Court needs to determine whether the applicant complied with the requirement to exhaust domestic remedies in respect of this part of the application, as required by Article 35 § 1 of the Convention, which, in its relevant parts, provides:

> "1. The Court may only deal with the matter after all domestic remedies have been exhausted, according to the generally recognised rules of international law ..."

637. The Court reiterates that the rule of exhaustion of domestic remedies under Article 35 § 1 of the Convention obliges applicants to use first the remedies which are available and sufficient in the domestic legal system to enable them to obtain redress for the breaches alleged. The

existence of the remedies must be sufficiently certain both in theory and in practice, failing which they will lack the requisite accessibility and effectiveness. Article 35 § 1 also requires that complaints intended to be brought subsequently before the Court should have been made to the appropriate domestic body, at least in substance and in compliance with the formal requirements and time-limits laid down in domestic law and, further, that any procedural means that might prevent a breach of the Convention should have been used. However, there is no obligation to have recourse to remedies which are inadequate or ineffective (see, for example, *Aksoy*, 18 December 1996, §§ 51-52, *Reports* 1996–VI; *Akdivar and Others v. Turkey*, 16 September 1996, §§ 65-67, *Reports* 1996-IV; and, more recently, *Cennet Ayhan and Mehmet Salih Ayhan v. Turkey*, no. 41964/98, § 64, 27 June 2006).

638. The Court has emphasised that the application of the rule of exhaustion of domestic remedies must make due allowance for the fact that it is being applied in the context of machinery for the protection of human rights that the Contracting States have agreed to set up. Accordingly, it has recognised that Article 35 § 1 must be applied with some degree of flexibility and without excessive formalism. It has further recognised that the rule of exhaustion is neither absolute nor capable of being applied automatically; for the purposes of reviewing whether it has been observed, it is essential to have regard to the circumstances of the individual case. This means, in particular, that the Court must take realistic account not only of the existence of formal remedies in the legal system of the Contracting State concerned but also of the general context in which they operate, as well as the particular circumstances of the applicant. It must then examine whether, in all the circumstances of the case, the applicant did everything that could reasonably be expected of him or her to exhaust domestic remedies (see *Akdivar and Others*, cited above, § 69; *Aksoy*, cited above, §§ 53-54; and *Tanrıkulu v. Turkey* [GC], no. 23763/94, § 82, ECHR 1999-IV).

639. The Court reiterates that at the admissibility stage of the proceedings the Government claimed that the applicant company had failed to exhaust domestic remedies in respect of the attachment and seizure of its assets pending the enforcement proceedings, the alleged failure by the bailiffs to grant the company access to the case in the enforcement proceedings, the bailiffs' alleged inaction in respect of the Sibneft shares, the orders to pay a 7% enforcement fee and the circumstances of the valuation and sale of OAO Yuganskneftegaz.

640. Having examined the case file and the parties' submissions, the Court finds that in the part concerning the attachment and seizure of the assets the applicant company properly exhausted the available domestic remedies by raising its grievances before the competent domestic courts. The attachment order of 15 April 2004 was reviewed and upheld by the Appeal Court on 2 July 2004 (see paragraph 92) and was also examined and

confirmed by the City Court in its decision of 23 April 2004 in the context of the examination of the company's request of 22 April 2004 (see paragraphs 96-97), and by the City Court and the Appeal Court on 23 April and 2 July 2004 respectively in the context of examination of the company's request for an injunction against the attachment (see paragraphs 101 and 102). The seizure order of 1 July 2004 was reviewed at first instance on 17 September 2004 and in cassation on 2 February 2005 (see paragraphs 116-120). The seizure of OAO Yuganskneftegaz on 14 July 2004 was reviewed by the courts at four instances, on 6, 9 August, 25 October and 17 December 2004 respectively (see paragraphs 137-146). As regards the seizure orders of 14 July 2004 concerning OAO Tomskneft-VNK and OAO Samaraneftegaz, the City Court upheld them by respective judgments of 13 August and 2 September 2004, whilst the Circuit Court confirmed this conclusion by the respective decisions of 5 November 2004 and 18 January 2005 (see paragraphs 147-155).

641. Admittedly, the applicant company did not complain about the attachment order of 15 April 2004 by way of cassation and omitted the appeal procedure when contesting the seizure of its subsidiaries on 1 July 2004 and the seizure order of 14 July 2004 concerning OAO Tomskneft-VNK and OAO Samaraneftegaz. The Court would note, however, that given the circumstances of the applicant company's tax case, its overall situation at the relevant time, the applicable domestic law and the courts' responses to the arguments put forward by the applicant company in those proceedings, it is clear that both the attachment order of 15 April 2004 and the subsequent seizure orders of 1 and 14 July 2004 have been properly examined and confirmed by the domestic courts at various levels of jurisdictions and it does not appear that the applicant company's complaints in this connection had any additional prospects of success, had the company not omitted the above-mentioned judicial instances.

642. As regards the complaints about a 7% enforcement fee, the Court observes that the applicant company was ordered to pay this fee for the years 2000-2003. The company's challenge to this fee was examined and dismissed by the courts at three instances only in respect of the year 2000 (see paragraphs 130-134), whilst its complaints about the payment of the fee for the year 2001 were examined only at first instance and in cassation (see paragraphs 177-187). Also, it is not entirely clear whether the applicant company brought court proceedings in respect of the entire amount of the fee for the year 2002 (see paragraphs 200-204) and whether it brought any proceedings against such an order for the year 2003 (see paragraph 221). The Court again finds that, given the similarity of the orders for payment of enforcement fees for the years 2000-2003 and in view of other relevant circumstances such as the applicable domestic law and the courts' answers to the company's arguments in respect of the fee for the year 2000, there is nothing in the Government's submissions to suggest that the applicant

company's complaints in this connection would have had any prospects of success had the applicant company appealed against them.

643. As regards the alleged failure by the bailiffs to grant the company access to the case in the enforcement proceedings and the bailiffs' alleged inaction in respect of the Sibneft shares, the Court notes that the above-mentioned grievances are entirely subsumed by the complaint concerning the method of enforcement of the tax debt and in particular the choice of OAO Yuganskneftegaz as the first asset to be sold in satisfaction of the tax claims. In this connection, the Court would note that the applicant company clearly exhausted the available domestic remedies as regards the seizure and the subsequent measures leading to the eventual sale of OAO Yuganskneftegaz (see paragraphs 137-146), and it is also clear that the relevant domestic law specifically disallowed the courts to rearrange or otherwise postpone the repayment of the debt (see paragraphs 471-477) if there were, as in the case at hand, pending tax proceedings against the debtor. Thus, the applicant company could not have been expected to bring separate court proceedings in this connection. Overall, it is clear to the Court that the applicant company used all the remedies that it could reasonably be expected to use in connection with this part of the application.

644. Thus, the Court finds that the applicant company has complied with the requirement to exhaust domestic remedies in respect of this part of the application and dismisses the Government's preliminary objection accordingly.

645. Turning to the substance of the applicant company's complaints, the Court notes that in April 2004, simultaneously with the Tax Assessment proceedings, the domestic authorities initiated enforcement proceedings aimed at securing their tax claims and later recovering the sums awarded by the courts as a result of the examination of these claims. They attached the company's assets located in Russia and later partly froze the company's domestic bank accounts and seized the shares of the applicant company's Russian subsidiaries. On 20 July 2004 it was decided to auction off the company's principal production subsidiary OAO Yuganskneftegaz, in satisfaction of the company's tax liability, which at the time amounted to RUB 106.182 billion (some EUR 3.005 billion). As a result of the proceedings with regard to the Tax Assessments 2001 and 2002, the company's debt to the tax authorities further increased and by the time the auction of OAO Yuganskneftegaz took place in December 2004 the company already owed the tax authorities some RUB 431.259 billion (some EUR 11.061 billion). In addition to the payments resulting from the Tax Assessments 2000-2003, the company was also required to pay the bailiffs a 7% enforcement fee on the overall amount of the debt.

646. The Court notes that the authorities used a variety of measures in connection with the enforcement of the debt, such as the attachment and freezing orders, the seizure orders, the orders to pay enforcement fees and

the compulsory auction procedure. Though each of these measures could be seen as a separate instance of interference with the applicant company's rights under Article 1 of Protocol No. 1, their common and ultimate goal was to force the company to meet its tax liabilities. Accordingly, the appropriate way to analyse this part of the application is to examine the enforcement proceedings in their entirety as one continuous event. The Court further notes that the enforcement measures in question fall to be analysed under the third rule of Article 1 of Protocol No. 1, which allows the member States to control the use of property in accordance with the general interest, by enforcing "such laws as [they] deem necessary to secure the payment of taxes or other contributions or penalties". It follows that the Court's task is to determine whether the State authorities complied with the Convention requirement of lawfulness and, if so, whether they struck a fair balance between the legitimate state interest in enforcing the tax debt in question and the protection of the applicant company's rights set forth in Article 1 of Protocol No. 1.

647. As regards the lawfulness of the measures in question, the Court has no reason to doubt that throughout the proceedings the actions of various authorities had a lawful basis and that the legal provisions in question were sufficiently precise and clear to meet the Convention standards concerning the quality of law. The attachment, freezing and seizure orders were reviewed by the domestic courts and found to have been lawful. Likewise, the 7% enforcement fee was upheld by the domestic courts and cannot be said to have been selective, given the domestic case-law cited by the Government. As regards the decisions leading to the forced sale of OAO Yuganskneftegaz at auction and the auction process itself, the Court notes that they too were reviewed and upheld by the domestic courts as lawful (see paragraphs 263 and 265) and there is nothing in the case file or the parties' submissions to cast doubt on these conclusions. The only question that remains is whether the enforcement measures were proportionate to the legitimate aim pursued.

648. In this connection the Court would reiterate that its task is to determine whether a fair balance was struck between the demands of the general interest of the public and the requirements of the protection of the individual's fundamental rights. It finds it natural that in the tax sphere the Contracting States should enjoy a wide margin of appreciation in order to implement their policies. Nevertheless, the Court cannot fail to exercise its power of review and must determine whether the requisite balance was maintained in a manner consonant with the applicant company's right to "the peaceful enjoyment of [its] possessions", within the meaning of the first sentence of Article 1 of Protocol No. 1.

649. At the outset the Court notes the background to this case and, in particular, the fact that the applicant company was one of the largest taxpayers in Russia and that it had been suspected and subsequently found

guilty of running a tax evasion scheme, committed consecutively in 2000-2003. From the parties' submissions and the case file it seems clear that the applicant company had no cash funds in its domestic accounts to pay its tax debts immediately, and in view of the nature and scale of the debt it was unlikely that any third party would agree to assist the company with a loan or some form of security. Regard being had to the scale of the tax evasion, the sums involved for the years 2000-2003, the fact under domestic law that they were payable almost at once after the production of the respective execution writ (see paragraph 471), and even taking into account the Court's previous findings in respect of the fines for the years 2000 and 2001, it was questionable whether at the time when the authorities decided to seize and auction OAO Yuganskneftegaz the company was at all solvent within the meaning of section 3 of the Insolvency (Bankruptcy) Act, which generally expected the solvent debtor to repay its debts "within three months of the date on which compliance should have occurred" (see paragraph 496).

650. In view of the above considerations, the Court finds that the crux of the applicant company's case did not lay in the attachment of its assets and cash as such, but rather and essentially in the speed with which the authorities demanded the company to pay, in the decision which had chosen the company's main production unit, OAO Yuganskneftegaz, as the item to be compulsorily auctioned in the first instance, and in the speed with which the auction had been carried out.

651. Given the paramount importance of the measures taken by the authorities to the applicant company's future, and notwithstanding the Government's wide margin of appreciation in this field, the Court is of the view that the authorities were obliged to take careful and explicit account of all relevant factors in the enforcement process. Such factors were to include, among other things, the character and the amount of the existing debt as well as of the pending and probable claims against the applicant company, the nature of the company's business and the relative weight of the company in the domestic economy, the company's current and probable economic situation and the assessment of its capacity to survive the enforcement proceedings. Furthermore, the economic and social implications of various enforcement options on the company and the various categories of stakeholders, the attitude of the company's management and owners and the actual conduct of the applicant company during the enforcement proceedings, including the merits of the offers that the applicant company may have made in connection with the enforcement were to be properly considered.

652. The Court notes that the authorities examined and made findings in respect of some of these factors (see, for instance, the findings in respect of the offers of shares in OAO Sibneft in paragraph 124 or the findings in respect of request for payment spread in paragraph 157), but it is clear that at no point in the enforcement proceedings did they make an explicit

assessment in respect of all of them. In particular, neither the seizure order of 14 July 2004, which set in motion the process of auctioning OAO Yuganskneftegaz (see paragraph 137), nor any of the subsequent decisions, including the judicial decisions in the context of the company's complaints against the actions of the bailiffs (see paragraphs 137-158), mentioned or discussed in any detail possible alternative methods of enforcement and the consequences that they might have on the future of the company.

653. The Court finds this aspect of the enforcement proceedings of utmost importance when striking a balance between the interests concerned, given that the sums that were already owed by the company in July 2004 made it rather obvious that the choice of OAO Yuganskneftegaz as the first item to be auctioned in satisfaction of the company's liability was capable of dealing a fatal blow to its ability to survive the tax claims and to continue its existence.

654. The Court accepts that the bailiffs were bound to follow the applicable domestic legislation which might limit the variety of options in the enforcement procedure. Nonetheless, the Court is of the view that, notwithstanding these constraints, the bailiffs still had a decisive freedom of choice, the exercise of which could either keep the company afloat or eventually lead to its demise. Although the Court, in principle, does not find the choice of OAO Yuganskneftegaz entirely unreasonable, especially in view of the overall amount of the tax-related debt and the pending as well as probable claims against the company, it is of the view that before definitively selecting for sale the asset that was the company's only hope of survival, the authorities should have given very serious consideration to other options, especially those that could mitigate the damage to the applicant company's structure. This was particularly so since all of the company's domestic assets had been attached by previous court orders (see paragraph 27), and were readily available, the company itself did not seem to have objected to their sale (see paragraph 159) and there had been virtually no risk of the company seriously opposing these actions.

655. The Court further notes one other factor which seriously affected the company's situation in the enforcement proceedings. The applicant company was subjected to a 7% enforcement fee in connection with the entire amount of its tax-related liability, which constituted an additional hefty sum of over RUB 43 billion (EUR 1.16 billion), the payment of which could not be suspended or rescheduled (see paragraphs 484-486). This was a flat-rate fee which the authorities apparently refused to reduce, and these sums had to be paid even before the company could begin repaying the main body of the debt (see paragraph 484). The fee was by its nature unrelated to the actual amount of the enforcement expenses borne by the bailiffs. Whilst the Court may accept that there is nothing wrong as a matter of principle with requiring a debtor to pay for the expenses relating to the enforcement of a debt or to threaten a debtor with a sanction to incite his or

her voluntary compliance with enforcement writs, in the circumstances of the case the resulting sum was completely out of proportion to the amount of the enforcement expenses which could have possibly been expected to be borne or had actually been borne by the bailiffs. Because of its rigid application, instead of inciting voluntary compliance, it contributed very seriously to the applicant company's demise.

656. Lastly, the Court would again emphasise that the authorities were unyieldingly inflexible as to the pace of the enforcement proceedings, acting very swiftly and constantly refusing to concede to the applicant company's demands for additional time. Admittedly, this rigidity may have resulted at least in part from the relevant requirements of the domestic law (see paragraphs 471, 481 and 489). Nevertheless, the Court finds that in the circumstances of the case such lack of flexibility had a negative overall effect on the conduct of the enforcement proceedings against the applicant company.

657. On the whole, given the pace of the enforcement proceedings, the obligation to pay the full enforcement fee and the authorities' failure to take proper account of the consequences of their actions, the Court finds that the domestic authorities failed to strike a fair balance between the legitimate aims sought and the measures employed.

658. To sum up, the Court concludes that there has been a violation of the applicant company's rights under Article 1 of Protocol No. 1 on account of the State's failure to strike a fair balance between the aims sought and the measures employed in the enforcement proceedings against the applicant company.

C. The complaint about the Government's intentions in the tax and enforcement proceedings against the applicant company

659. The Court notes that, in addition to various specific grievances about the tax and enforcement proceedings already mentioned above, the applicant company also argued that the overall effect of these proceedings showed that the Government had brought and conducted the proceedings with the intent to destroy the company and to take control of its assets.

660. The Court will examine this part of the application under Article 18 of the Convention, taken in conjunction with Article 1 of Protocol No. 1.

Article 18 of the Convention

> "The restrictions permitted under [the] Convention to the said rights and freedoms shall not be applied for any purpose other than those for which they have been prescribed."

1. The applicant company's submissions

661. The applicant company argued that the circumstances of the tax assessment and enforcement proceedings as well as the allegedly "political" motivation behind the prosecution of Mr M. Khodorkovskiy and other owners and senior officials of the applicant company showed that the proceedings against it, taken as a whole, were abusive in that the State clearly wanted to destroy the company and to take control of its assets.

2. The Government's submissions

662. The Government disagreed, having maintained that tax assessment and subsequent enforcement proceedings had been lawful and regular and that the applicant company's demise was the direct result of its carrying out over many years a gigantic tax fraud.

3. The Court's assessment

663. The Court reiterates that Article 18 of the Convention does not have an autonomous role. This provision can only be applied in conjunction with the Convention provisions protecting substantive rights. It also follows from the terms of Article 18 that a violation can only arise where the right or freedom concerned is subject to restrictions permitted under the Convention (see, for example, *Gusinskiy v. Russia*, no. 70276/01, § 73, ECHR 2004-IV). The Court further notes that in order to hold a member State liable under this provision an applicant should be able to furnish the Court with an incontrovertible and direct proof in support of his or her allegations.

664. The Court would observe that in its previous analysis under Article 6 of the Convention and Article 1 of Protocol No. 1 it has already addressed the applicant company's points about the nature of its debt to the authorities, and in particular the merits of the 2000-2003 Tax Assessments proceedings. Despite the fact that it found a violation of Article 6 of the Convention on account of the speed with which the courts had conducted the proceedings in the 2000 Tax Assessment case and a violation of Article 1 of Protocol No. 1 on account of the interference by the Constitutional Court with the outcome of the 2000 Tax Assessment case in the part relating to penalties, the Court rejected the applicant company's claims that the company's debt had been recognised as a result of an unforeseeable, unlawful and arbitrary interpretation of the domestic law (see paragraphs 605 and 616). The Court also recognised the right of the State to enforce, as such, the court judgments, but reached conclusions concerning the handling of the enforcement proceedings by the domestic authorities which lead to the finding of a violation of Article 1 of Protocol No. 1. In view of these findings, the Court will proceed on the assumption that the company's debt in the enforcement proceedings resulted from legitimate

actions by the respondent Government to counter the company's tax evasion and the burden of proof would accordingly rest on the applicant company to substantiate its allegations.

665. Regard being had to the case file and the parties' submissions, including the applicant company's references to the allegedly political motivation behind the prosecution of the applicant company and its owners and officials, the Court finds that it is true that the case attracted massive public attention and that comments of different sorts were made by various bodies and individuals in this connection. The fact remains, however, that those statements were made within their respective context and that as such they are of little evidentiary value for the purposes of Article 18 of the Convention. Apart from the findings already made earlier, the Court finds no indication of any further issues or defects in the proceedings against the applicant company which would enable it conclude that there has been a breach of Article 18 of the Convention on account of the applicant company's claim that the State had misused those proceedings with a view to destroying the company and taking control of its assets.

666. To sum up, the Court finds that there has been no violation of Article 18 of the Convention, taken in conjunction with Article 1 of Protocol No. 1, on account of the alleged disguised expropriation of the company's property and the alleged intentional destruction of the company itself.

D. Alleged violations of Articles 7 and 13 of the Convention

667. Regard being had to the particular circumstances of the present case and to the reasoning which led it to find a violation of Article 6 of the Convention and Article 1 of Protocol No. 1 to the Convention, the Court finds that there is no cause for a separate examination of the same facts from the standpoint of Article 7 of the Convention and through the prism of the "effective remedies" requirement of Article 13.

IV. APPLICATION OF ARTICLE 41 OF THE CONVENTION

668. Article 41 of the Convention provides:

> "If the Court finds that there has been a violation of the Convention or the Protocols thereto, and if the internal law of the High Contracting Party concerned allows only partial reparation to be made, the Court shall, if necessary, afford just satisfaction to the injured party."

669. The applicant company claimed a lump sum of over 81 billion euros and a daily interest payment of EUR 29,577,848 in respect of pecuniary damage, "no less than 100,000 euros" in respect of non-pecuniary damage and EUR 171,444.60 in respect of costs and expenses.

670. The Government disagreed, having contested both the authority of Mr Gardner to make the Article 41 claims on behalf of the applicant company as well as the well-foundedness of the calculations in question.

671. The Court considers that the question of the application of Article 41 is not ready for decision. Accordingly, it shall be reserved and the subsequent procedure fixed having regard to any agreement which might be reached between the applicant company and the respondent Government (Rule 75 § 1 of the Rules of Court).

FOR THESE REASONS, THE COURT

1. *Finds* by six votes to one that the Court is not barred, pursuant to Article 35 § 2 (b) of the Convention, from examining the merits of the case;

2. *Holds* by six votes to one that there has been a violation of Article 6 § 1 and 3 (b) of the Convention as regards the 2000 Tax Assessment proceedings on account of the insufficient time available to the applicant company for preparation of the case at first instance and on appeal;

3. *Holds* by four votes to three that there has been a violation of Article 1 of Protocol No. 1 on account of the 2000-2001 Tax Assessments in the part relating to the imposition and calculation of penalties;

4. *Holds* unanimously that there has been no violation of Article 1 of Protocol No. 1 as regards the rest of the 2000-2003 Tax Assessments;

5. *Holds* unanimously that there has been no violation of Article 14 of the Convention, taken in conjunction with Article 1 of Protocol No. 1;

6. *Dismisses* by a majority the Government's preliminary objection as to the exhaustion of the domestic remedies in respect of the attachment and seizure of the applicant company's assets pending the enforcement proceedings, the alleged failure by the bailiffs to grant the company access to the case in the enforcement proceedings, the bailiffs' alleged inaction in respect of the Sibneft shares, the orders to pay a 7% enforcement fee and the circumstances of the valuation and sale of OAO Yuganskneftegaz; and

7. *Holds* by five votes to two that there has been a violation of the applicant company's rights under Article 1 of Protocol No. 1 in the enforcement proceedings against the applicant company in that the domestic

authorities failed to strike a fair balance between the legitimate aim of these proceedings and the measures employed;

8. *Holds* unanimously that there has been no violation of Article 18, taken in conjunction with Article 1 of Protocol No. 1;

9. *Holds* unanimously that in view of its previous conclusions under Article 6 of the Convention and Article 1 of Protocol No. 1 the case requires no separate examination under Articles 7 and 13 of the Convention;

10. *Holds* unanimously that the question of the application of Article 41 is not ready for decision;
accordingly,
(a) *reserves* the said question in whole;
(b) *invites* the parties to submit, within three months from the date on which the judgment becomes final in accordance with Article 44 § 2 of the Convention, their written observations on the matter and, in particular, to notify the Court of any agreement that they may reach;
(c) *reserves* the further procedure and *delegates* to the President of the Chamber the power to fix the same if need be.

Done in English, and notified in writing on 20 September 2011, pursuant to Rule 77 §§ 2 and 3 of the Rules of Court.

Søren Nielsen	Christos Rozakis
Registrar	President

In accordance with Article 45 § 2 of the Convention and Rule 74 § 2 of the Rules of Court, the following separate opinions are annexed to this judgment:
(a) Partly dissenting opinion of Judge Jebens;
(b) Partly dissenting opinion of Judge Hajiyev and Judge Bushev.

C.R.
S.N.

PARTLY DISSENTING OPINION OF JUDGE JEBENS

I respectfully disagree with the opinion expressed by the majority that there has been a violation of Article 1 of Protocol No. 1 in this case in respect of the 2000-2001 Tax Assessments with regard to the imposition and calculation of penalties.

I find it useful to clarify the legal questions and give an outline of the developments in the domestic case-law before explaining my opinion in the case.

The legal question before the Court and the developments in the domestic case-law with respect to the imposition of penalties for tax evasion

The applicant company complains that the imposition of tax penalties violated its right to protection of property, which is secured by Article 1 of Protocol No. 1 to the Convention. It should be noted that the question before the Court in this respect is not whether there was a legal basis in domestic law for imposing penalties on the company for acts of tax evasion, but whether the imposition of penalties was precluded. The applicant company argues that prosecution for the alleged tax evasion had become time-barred, in that the decision which established its outstanding tax liability for the year 2000 and imposed a requirement to pay tax arrears, default interest and penalties was adopted on 14 April 2004, that is, outside the time-limit set out by the legislation.

The relevant provision, namely Article 113 of the Tax Code, provided for a three-year time-limit for holding a taxpayer liable for tax offences. Under the domestic courts' practice, that period ran from the first day after expiry of the relevant tax term and ended when the taxpayer was held liable. However, the part of their interpretation of the provision which referred to the end of the period in question was the subject of several subsequent clarifications by the superior domestic courts.

In its resolution of 28 February 2001 the Plenum of the Supreme Commercial Court indicated to the lower commercial courts that "a taxpayer is considered to have been held liable (within the meaning of Article 113 of the Tax Code) on the date on which the head of the (relevant) tax body or his deputy takes a decision to hold this person liable for a tax offence in accordance with (the rules set out in) the Code" (see paragraph 405 of the judgment). This interpretation was subsequently applied by the lower commercial courts. However, while it generally secured a fair balance between the interests of the tax authorities and those of taxpayers, it would seem to be problematic in situations where the taxpayer impeded the

inspections by the tax authorities and thereby delayed the adoption of the relevant decision with regard to the time-limit in Article 113.

In the present case several of the applicant company's subsidiaries had refused to comply at all, while others had failed to provide the documents on oil transactions which the tax authorities had requested during the on-site inspection (see paragraph 17 of the judgment). The lower courts held that in such situations the rules on the statutory time-bar were inapplicable, because the applicant company had acted in bad faith. This opinion was not upheld by the supervisory review instance, which pointed out that setting aside the time-limits would be in clear contradiction of the legislation and the relevant case-law. It therefore referred the issue to the Presidium of the Supreme Commercial Court, which referred it to the Constitutional Court (see paragraph 564).

In its decision of 14 July 2005 the Constitutional Court clarified, firstly, that the rules on time limitation for imposing penalties should apply in any event, regardless of whether the taxpayer had acted in "bad faith". It went on to note that, exceptionally, if the taxpayer had impeded the tax authorities' inspections and thereby delayed the adoption of the relevant decision, the running of the time-limit could be suspended by the adoption of a tax-audit report, setting out the circumstances of the tax offence in question and referring to the relevant articles of the Tax Code (see paragraph 565).

Whether there has been a violation of Article 1 of Protocol No. 1

The applicant company complains about the imposition and calculation of tax penalties, but they do not claim that the decision to impose tax penalties lacked a substantive legal basis. There can be no doubt that such a basis existed in the Russian legislation (see Articles 112 § 2 and 114 § 4 of the Tax Code), and that the provision in question was sufficiently clear and foreseeable (see paragraphs 400-402).

Furthermore, although the clarification provided by the Constitutional Court implied a change in the interpretation of Article 113, it was consistent with the essence of the offence and did not broaden the scope of offences which could lead to prosecution for tax evasion and imposition of penalties. It is important that the novel interpretation of Article 113 did not set aside the rules on time limitations for the imposition of penalties due to tax evasion, nor did it shorten the time-limits for the imposition of such measures. In fact, the Constitutional Court merely explained the existing rules on time-limits in order to ensure their fair application to taxpayers who acted improperly.

As regards the foreseeability of the measure, the matter should be seen in the light of the applicant's individual situation as well as the evolution of the Constitutional Court's jurisprudence in this sphere. The tax inspection in respect of the applicant company for the year 2000 was instituted in December 2003, and the audit report was adopted and served on the company on 29 December 2003; in other words, both those events occurred within the three-year time-limit specified in Article 113. Therefore, by that date, the company could already have reasonably expected that it was likely to face substantial penalties in connection with tax evasion.

It should also be noted that the acts in question constituted tax offences at the time when they were committed and that the penalties requested by the Ministry and eventually imposed by the courts were not heavier than those applicable at that time (compare *Coëme and Others v. Belgium*, cited above, § 150). Finally, it is of relevance that the decision of 14 April 2004 was based on the same facts and the same application of the Tax Code as the audit report of 29 December 2003. It remains the fact that the applicant company hoped to avoid liability for tax evasion by actively impeding the tax inspections and delaying the adoption of the relevant decision by the tax authorities (paragraph 17). However, that in itself is, in my view, insufficient to merit protection, given the circumstances of the case.

In addition, the concept of "good faith" within the field of tax legislation and practice was not an entirely novel one. The Constitutional Court first used the concept of "good faith" when assessing the conduct of taxpayers in their relations with tax officials as early as 1998. It subsequently expanded on this notion, explaining in 2001 that there existed a refutable presumption that the taxpayer was acting in good faith and that a finding that a taxpayer had acted in bad faith could have unfavourable legal consequences for the taxpayer. In view of the evolution of the Constitutional Court's jurisprudence in this sphere (see paragraphs 384-387), the applicant company could, in my opinion, have foreseen that its actions to delay the tax inspection could qualify as bad-faith conduct.

Referring to the circumstances of the case as explained above, the development in the superior domestic courts' interpretation of the provisions in question and the State's wide margin of appreciation in this sphere, I conclude that the Tax Assessment for 2000-2001 and the imposition of penalties complied with the requirement of lawfulness of Article 1 of Protocol No. 1.

PARTLY DISSENTING OPINION OF JUDGE BUSHEV, JOINED IN PART BY JUDGE HAJIYEV

The present opinion contains the joint dissenting opinion of Judge Hajiyev and of Judge Bushev with regard to the finding of a violation of Article 1 of Protocol 1 to the Convention (parts 1 and 2 below), and that of Judge Bushev with regard to the remainder of the issues (parts 3 and 4 below).

As to the violation of Article 1 of Protocol 1 to the Convention

Unfortunately, we must dissent from our colleagues' (hereinafter, the Court) finding that there was a violation of Article 1 of Protocol 1 to the Convention in the case at hand, concerning (1) application of the 3-year limitation period, provided by article 113 of the Tax Code of the Russian Federation, in respect of the imposition of penalties for the years 2000 and 2001, and in respect of (2) certain elements of the enforcement proceedings with regard to court judgments on the debt arising from the Tax Assessments 2000-2003 (hereinafter, the enforcement procedure).

We will now examine each of the aforementioned findings.

1. With regard to application of the 3-year limitation period in respect of the imposition of penalties for the years 2000 and 2001.

1.1. The Court has, in essence, agreed in full with the conclusions of the Russian courts that OAO Neftyanaya kompaniya Yukos (hereinafter, Yukos) conducted numerous illicit transactions for the sole purpose of systematically and intentionally evading the payment of taxes. In addition, the Court found that the corresponding tax legislation, in form and in content, and the actions of the authorities in pursuing the assessment of tax arrears and surcharges, fully met the high standards of the Convention. Thus, the Russian Government had enough reasonable grounds for levying taxes and surcharges from the applicant. Equally, the Court has not challenged the Russian Government's finding that Yukos actively opposed tax inspections, thus acting *mala fides*, for the purpose of drawing out the time-limits for their performance.

1.2. As to the levying of penalties for the intentional tax evasion, the Court did not find the rates applied excessively high or disproportional (see § 606 of the judgment). However, the Court's findings with respect to each of the three tax periods differ, depending on the possibility of applying the 3-year limitation period set out in Article 113 of the Tax Code, to the imposition of tax liability.

· Thus, with respect to the penalties imposed in April 2004 for the tax violations committed in the period 2002-2003, the Court has not found any violations of the Convention, since those periods fall within the 3-year limitation period.

· In accordance with the rules of application of the 3-year limitation period identified by the Court, it found that imposition of the penalties in 2004 for the tax violations committed in 2000 contradicts the requirements of Article 113 of the Tax Code.

· With regard to the third period, concerning the penalties for 2001, the Court, while not doubting the grounds for their imposition, nonetheless challenged the 80 % rate of the penalty. The Court was not convinced by the Government's argument that, under Article 114 of the Tax Code, the penalty could be increased from 40% to 80% in the event of a repeat conviction. Indeed, following the Court's logic on the limitation period applicable to the penalties for 2000, there was no repetition in 2001, due to the fact that 2001, not 2000, is the first year for which the limitation period is inapplicable. In other words, the penalties for 2000 could not be treated as the initial instance of imposition of tax liability, and therefore, the increase in the penalty rate from 40% to 80% in 2001 was inadmissible, given that there was no repetition of the offence, for which liability could be imposed.

1.3. In examining the rule on the limitation period set out in Article 113 of the Tax Code, the Court has taken a literal approach, which has led it to find that neither the given provision, nor any other provisions of Russian legislation set out a ground for suspending or amending the limitation period. In the Court's opinion, the wording of Article 113 of the Tax Code does not render it possible to foresee any exceptions from the rule arising from certain circumstances. In particular, the Court has not supported the Government's argument that bad faith on the part of the taxpayer, expressed by actively opposing the authorities in establishing and classifying all elements of the corresponding fiscal and legal relationship, is such an exception.

The Court thus considers that the rule set out in Article 113 of the Tax Code did not render it possible for a reasonable person with a fair degree of certainty to foresee any inapplicability of the 3-year limitation period, even where such a person was actively impeding the tax authorities. Hence, as regards the penalties for 2000, the Court believes that the "quality" of Article 113 of the Tax Code did not meet in full the requirement of lawfulness for the Government's interference in private property.

1.4. We are not convinced by the Court's arguments.

Indeed, the lawfulness criterion is an indispensable requirement in appraising a Government's activity in the light of Article 1 of Protocol 1 to

the Convention. For this purpose the notion of law has a wide meaning and includes not only the acts of the respective parliament, but also delegated legislation, decrees, court practice, etc. The law has to meet certain requirements as to its form and substance. One of the requirements imposed on law under the Convention is its legal certainty, rendering it possible for private persons and public authorities to foresee the legal consequences of particular conduct. Meanwhile, the case-law of the European Court on Human Rights (the ECHR) follows the assumption that "those consequences need not be foreseeable with absolute certainty: experience shows this to be unattainable" (see *Rekvényi v. Hungary* [GC], no. 25390/94, § 34, ECHR 1999-III and *Hertel v. Switzerland*, 25 August 1998, § 35, *Reports of Judgments and Decisions* 1998-VI, refer also to § 598 of the judgment).

We believe that in the case at hand the statutory wording (its "quality"), and the specific qualities of the offender were reasonable enough for it to foresee the probability that the limitation rules set out in Article 113 of the Tax Code might be inapplicable in the event of its actively opposing (obstructing) tax inspections. Let us clarify this thinking.

1.5. "Legal quality" of Article 113 of the Tax Code.

No legal system enables the domestic legislation to be descriptive enough to provide for every eventuality. Setting out a rule of conduct in statute and comprehending the implicit sense thereof is attained by virtue of various legal techniques, including, in particular, judicial interpretation, the interpretation of a rule within a system of other rules, etc. Russian legislation has been codified in the traditions of a pandectic system of law, which assumes that comprehension of the implicit sense of a given special rule can be provided often by taking into consideration a more general rule. A general rule is by default applicable to a special rule, unless the latter sets out directly (obviously) an exception (waiver) to the former. In such a codification system the interpretation principles assume that every special rule contains the provisions of a more general rule, although the literal text of the said general rule is not included in the literal text of a special rule for the purposes of legal techniques.

Moreover, in the pandectic system a comprehension of the implicit sense of either special or general rules ought to exist through legal principles, which have a universal and exhaustive role. The effect of a legal principle is assumed with respect to each rule of the respective branch of law; every single rule set out in legislation is to be comprehended and applied within the semantic borders of the legal principle and unless the former contradicts the latter.

1.6. One such general legal principle is the principle of non-abuse of one's rights and the consequent principle of refusal to grant protection to a

person who has abused his or her rights. This principle is directly set out in the provisions of the branch of law which regulates property relationships and in the closely-related tax legislation.

Thus, under Article 17 (3) of the Constitution of the Russian Federation, which is applicable directly to any relationship (Article 15(1)), the exercise of individual and civic rights and freedoms must not violate the rights and freedoms of others. As provided by Article 10 of the Russian Civil Code (this rule came in effect in 1995), which regulates property relationships in general, "actions by citizens and legal entities, performed with the express purpose of inflicting damage to another person, and the abuse of civil rights in other forms shall be inadmissible" (paragraph 1), and where a person fails to abide by this requirement a court shall have the right to reject this person's claim for the protection of that right (paragraph 2).

1.7. With regard to tax relationships, the Russian Constitutional Court has drawn attention to the necessity, in elucidating the special rules of tax legislation, of applying the principle of refusal of protection of rights to persons abusing those rights. The present interpretation was given by the Constitutional Court both prior to the commission of tax violations by Yukos in 2000 (Constitutional Court judgment no. 24-P of 12 October 1998) and in the course of the limitation period, when the applicant was actively impeding the tax inspection (Constitutional Court judgment no. 139-O of 25 July 2001, etc.). The Court on the other issue has also acknowledged the possibility of uncertainty in the law, including the criminal law, as well as, in essence, a need to apply the legal principles – when assessing the quality of the law on specific taxes (see § 598 in the judgment).

1.8. Apart from those principles, consideration should be given to a special rule in Russian legislation which could be used in comprehending the implied sense of Article 113 of the Tax Code. Thus, the Court believes that the high rate of penalties (40%) applicable in cases of intentional tax violation creates a similarity between this sanction and measures imposed under the criminal law. Therefore, the Court argues, where such tax liability is imposed, procedural guarantees similar to those applicable in cases of criminal liability should be granted. This conclusion by the Court in respect of the present case is extremely debatable (see paragraphs 3.2 – 3.4 below). Nonetheless, the key issue lies elsewhere. If we follow the Court's logic, the offender, in assessing the risk of applicability of the limitation period to its case, ought also, in our view, to have (or, at least, could reasonably have) considered the special rule of criminal law. According to Article 78 (3) of the 1996 Criminal Code, "expiry of a limitation period shall be suspended if the person who has committed the crime impedes the investigation or court trial".

Besides, the rules on suspension or amendment of the limitation period as a result of certain exceptional circumstances are applicable and ultimately similar for all forms of legal liability.

1.9. Thus, Russian legislation contained provisions with sufficient legal certainty for the purpose of foreseeing the consequences of bad faith in opposing tax inspections and the applicability of a limitation period in this regard.

1.10. The Court in its judgment points to certain circumstances that *prima facie* diminish the "quality" of law and decrease the legal certainty of Article 113 of the Tax Code. Among such circumstances the Court refers to (i) paragraph 36 of judgment no. 5 of the Supreme Arbitration (Commercial) Court Plenum of 28 February 2001 ((§ 405), hereinafter – the SAC judgment of 2001), (ii) the Constitutional Court's decision of 18 January 2005 ((§ 75), hereinafter – CC Decision of 2005), (iii) the Constitutional Court's judgment of 14 July 2005 (hereinafter – the CC Judgment of 2005) and, last but not least, (iv) amendments to Article 113 of the Tax Code adopted in Federal Law no. 137-FZ of 27 July 2006 ((§ 410), hereinafter – the 2006 Federal Law). Although all of these circumstances pertain to Article 113 of the Tax Code, their quantity should not affect the comprehension of the "legal quality" of the provision at hand.

In fact, the SAC judgment of 2001 eliminated internal inconsistencies and contradictory court practice regarding the point at which tax liability is imposed (either the point of drawing up a record of a violation, or the point of adopting a resolution on the imposition of tax liability). The issue of bad faith in impeding tax inspections, and the applicability of the limitation period in this regard, was not addressed in the judgment. Neither was it touched upon in the CC Decision of 2005, which affirmatively answered a request by Yukos regarding the relevance of the limitation period's application *per se*. The Constitutional Court justified its refusal to examine Yukos's claim on the ground that it was inadmissible, as the applicant sought reassessment of the facts as stated by the arbitration (commercial) court, a matter that does not fall within the Constitutional Court's authority (paragraph 2 of the CC Decision of 2005, paragraph 1.3 of the CC Judgment of 2005).

The CC Judgment of 2005 confirmed the Constitutional Court's previous finding on the refusal of protection to bad-faith taxpayers, drawing attention to the fact that the said universal principle was also to be applied for the purpose of ascertaining the implicit sense of Article 113 of the Tax Code. Furthermore, the Constitutional Court emphasised that conduct such as impeding a tax inspection might be treated as a taxpayer's abuse of rights and ought to be regarded as a certain form of bad-faith conduct by the taxpayer. The CC Judgment of 2005 indisputably increased legal certainty

in comprehension of the special rule of Article 113 of the Tax Code and thus raised the degree of protection for the property interests of private persons. A comparable effect was gained through the enactment of the 2006 Federal Law. Nevertheless, the same interpretation was reasonably foreseeable on the basis of the previously existing legislative provisions, and the "legal quality" thereof complied fully with the requirements of the Convention.

1.11. The applicant's subjective ability to comprehend the implicit sense of the law.

In deciding in any given case whether there has been a violation of the Convention in respect of the applicant, the ECHR considers that applicant's specific situation. Evidently, applicants' individual ability to interact with the public authorities, the degree of their security, so to speak, their ability to have victim status for the purposes of the Convention, can differ substantially. Nevertheless, in spite of its case-law, the Court in the case at hand failed to examine and refused to consider Yukos' subjective ability to foresee the consequences of its own conduct in actively impeding tax inspections, and to assess the explicit and implicit sense of Article 113 of the Tax Code. Such approach by the Court is not consistent, as on the other issue – assessment of quality of provisions of the special tax laws, i.e. of an element of the tax law offence – the Court has taken into consideration the fact that the applicant was a large holding, capable to consult with experts for risk assessments (see § 599 of the judgment).

1.12. Yukos was one of the largest commercial companies in Russia. Running a business (carrying out for-profit activities) at one's own risks implies consent by a commercial company, in the person of its managing bodies, to accept various consequences resulting from conditions of uncertainty, including the imperfections of legislation. The consequences of such uncertainty might be either positive or negative. Therefore, in regulating relationships involving non-entrepreneurs, especially physical persons (humans), who are able to influence the consequences of their risk to a lesser degree than commercial companies, the legal certainty of legislation should be substantially higher than for entrepreneurs (commercial companies). To paraphrase the above-mentioned principle, for the purposes of the Convention the standard of legal certainty of a legal rule might be lower for commercial companies.

It is undeniable that the applicant possessed an extremely high potential to assess its own legal risks; its consultants (advisors) were able to reasonably foresee all the possible consequences of application of a legal rule. One need only note that in certain proceedings the applicant was represented by 8 to 10 professional lawyers, the company carried out large-scale and legally significant activities both in Russia and abroad,

implementing legal solutions that were occasionally unorthodox in the Russian legal sphere (e.g. use of transnational jurisdiction, the creation of multidivisional branches of affiliates (including sham companies) within a large Russian territory, as well as abroad). It should be mentioned that the applicant was aware of the possibility of tax liability well in advance of the expiry of the 3-year limitation period (a long-term tax inspection preceded signing the protocol on 29 December 2003, establishing tax-law violations); the decision imposing tax liability was issued with an insignificant overstepping of the 3-year term (14 April 2004, i.e. 3 and a half months); the tax authorities filed a claim for tax penalties on 14 April 2004, i.e. within the general term for public authorities to respond to tax violations, namely 3 years (the limitation period under Article 113 of the Tax Code) plus 6 months (the term for bringing a lawsuit before a court, Article 115 of the Tax Code).

1.13. Thus, we believe that neither the "quality" of the tax legislation (the objective factor), nor the alleged legal uncertainty with respect to the applicant's rights (the subjective factor) constituted a violation of Article 1 of Protocol 1 to the Convention in terms of the existence of lawful grounds for an insignificant prolongation of the limitation period for the penalties in respect of 2000.

1.14. Retrospective effect of the CC Judgment of 2005.

We were also not convinced by the Court's evaluation of the significance of the retrospective effect of the CC Judgment of 2005 with regard to interpretation of Article 113 of the Tax Code. As was mentioned above, the Constitutional Court did not amend the rules on application of the limitation period, it merely increased legal certainty in comprehension of the special rule of Article 113 of the Tax Code, which, in turn, had been reasonably foreseeable. However, even if we assume that the Constitutional Court introduced a new rule on the influence of a taxpayer's bad faith on the running of the limitation period, the retrospective application of such a "new" rule was admissible in the given circumstances.

The Convention recognizes a wide margin of appreciation for national governments in regulating taxation and levying taxes and *penalties*. The ECHR respects any decision by the national legislator in this sphere, unless such a decision obviously has no reasonable ground (see *Gasus Dosier- und Fördertechnik GmbH v. the Netherlands*, 23 February 1995, § 60, Series A no. 306-B). The ECHR's case-law contains several instances where the Court accepted retrospective amendments to legislation and, correspondingly, the imposition of additional payments on taxpayers (see *National & Provincial Building Society, Leeds Permanent Building Society and Yorkshire Building Society v. the United Kingdom*, 23 October 1997,

§ 80, *Reports of Judgments and Decisions* 1997-VII, *Di Belmonte v. Italy*, no. 72638/01, 16 March 2010).

It is worth noting that in the instant case the Constitutional Court did not stipulate any additional obligations regarding the rules on charging and paying taxes, nor did it impose a different rate of tax liability. At the moment of committing the tax offence the applicant had been aware of all of the principal conditions for imposing liability. It is unlikely that establishment of a limitation period is aimed at preventing or correcting the socially undesirable conduct of private individuals. Considering the vast amounts of evaded taxes and the long-term period of the tax violations, it is hardly reasonable to assume that the applicant would have not begun evading taxes or impeding tax inspections if it had been aware that the limitation period might have been 3 years and three-and-a-half months rather than 3 years.

1.15. Finally, let us end with a reference to the judgment of 17 May 2010 in the case of *Kononov v. Latvia*, delivered by the Grand Chamber, in which the Court set out certain standards as to the legal certainty and foreseeability of a legal rule. We would recall that the issue in question in this case was the legal certainty of a rule which had been effective in the distant past and which became the legal ground for imprisonment of the applicant for 6 years in 2000 for "military crimes" committed, according to the Latvian authorities, in 1944. At the moment when the events under consideration occurred, Latvian criminal legislation did not contain any explicit provisions regarding military crimes; moreover, it stipulated general and special limitation periods for criminal liability. Those limitation periods had expired long before the beginning of the criminal proceedings against Kononov. In 1993 the provisions on limitation periods were abolished by a Latvian legislative act. Nevertheless, the ECHR held that serviceman Kononov, who, unlike the applicant in the present case, had no real opportunity to apply to consult legal advisers, relying on a combination of various international conventions and legal customs (including certain that were not officially promulgated) *could* have foreseen that his conduct might be qualified as a military crime. In this the ECHR was also not troubled by the fact that the limitation period set out in national legislation for any type of crime at the time when Kononov committed the alleged offence (1944) had expired several decades before Kononov was brought to trial in 2000 (see *Kononov v. Latvia* [GC], no. 36376/04, § 239, 17 May 2010).

The right to liberty is one of the most protected rights under the Convention; it is at the summit in the hierarchy of human rights values, and therefore the standard of legal certainty in respect of it is much higher than in respect of the rules entitling national governments to control the private property of business organisations in the form of levying taxes and penalties.

1.16. The ECHR has repeatedly ruled that the burden of interpretation and enforcement of national legislation is primarily with the competence of national public authorities, and particularly state courts (see *Winterwerp v. the Netherlands*, 24 October 1979, § 60, Series A no. 33 and *Iglesias Gil and A.U.I. v. Spain*, no. 56673/00, § 61, ECHR 2003-V). In the case at issue the legal interpretation was given by the Constitutional Court; that interpretation is based on reasonable grounds, is not evidently unsubstantiated or unjust, and, considering the judgment in the Kononov case and the remainder of the case-law, meets the requirements of the Convention.

2. With regard to the enforcement proceedings.

2.1. In assessing the Government's actions to collect tax arrears from Yukos the Court found no breaches of national law; however, the Court held that the measures taken by the public authorities against the offending company were disproportionate (see § 647 of the judgment). According to the Court, the enforcement procedure was executed too rapidly, the applicant in fact had been provided no real opportunity for any alternative ways to pay off its tax debts, the forfeiture of stocks in OAO Yuganskneftegaz (OAO "YNG") (the applicant's primary business asset) by auction was not justified, etc. (§ 650). At the same time, the Court did not find every single element of the enforcement proceedings to be disproportionate, but only in the cumulative effect of such elements. Further, in the Court's opinion, the State did not properly take into consideration all of the factors related to the enforcement proceedings (§ 651), though it accounted a few of those (§ 652).

2.2. The width of the State's margin of appreciation and factors determining its bounderies.

We would reiterate that the ECHR's case-law relies on the necessity of recognising the wide margin of appreciation enjoyed by national governments in deciding on the exact measures intended to guarantee observance of human rights. The bounds of such discretion can vary depending on the scope and the nature of a certain right, as well as other circumstances developed under the ECHR's practice (see *Buckley v. the United Kingdom*, 25 September 1996, § 74, *Reports of Judgments and Decisions* 1996-IV). For the purposes of levying taxes and penalties a government's margin of appreciation is deemed to be particularly wide (see § 648 of the judgment).

The ECHR demonstrates even more tolerance towards the public authorities' actions in respect of private persons in cases where **(a)** an applicant happens to be a commercial company (see *Špaček, s.r.o., v. the Czech Republic*, no. 26449/95, § 59, 9 November 1999, *Regent Company v.*

Ukraine, no. 773/03, §§ 60, 61 and 67, 3 April 2008). **(b)** an applicant's conduct contributed to his detriment (see *Beyeler v. Italy* [GC], no. 33202/96, § 116, ECHR 2000-I) **(c)** the applicant behaved unfairly - *mala fides* (see *AGOSI v. the United Kingdom*, 24 October 1986, § 54, Series A no. 108, *Sarmin and Sarmina v. Russia* (dec.), no. 58830/00, 22 November 2005, *Al-Nashif v. Bulgaria*, no. 50963/99, § 89, 20 June 2002); **(d)** there is no consensus among the Contracting States, i.e. governments employ different measures under similar circumstances (see *T. v. the United Kingdom* [GC], no. 24724/94, §§ 71-72, 16 December 1999), etc. Moreover, the ECHR considers the specific economic and other circumstances in which the governmental action being assessed was carried out (see *James and Others v. the United Kingdom*, 21 February 1986, § 46, Series A no. 98).

All of these factors, developed in the ECHR's case-law and cumulatively denoting a need to recognize a much wider margin of appreciation for the Government than in other cases, are present here. However, they have not been taken into consideration properly by the Court.

2.3. Yukos at that time was one of the biggest commercial companies, not only in Russia, but throughout the world, and wielded considerable economic and other influence and power. The company engineered and implemented large-scale abusive tax schemes for the sole purpose of systematically and intentionally evading taxes. As a result, the State budget suffered a tremendous amount of damage, unprecedented in the area of tax violations. In the meantime the unpaid funds were at the company's disposal, having probably enriched substantially both the company and its shareholders. The Government's actions were aimed only at levying tax arrears and penalties (see § 646 of the judgment) the alleged political motive, and the aim of reallocating assets or another intention, unrelated to the tax collection, and selectiveness (discrimination) by the State, as claimed by the applicant, were held to be unsubstantiated (§§ 616, 666). The scope and rapidity of the State measures against the applicant were determined by the scale of intentional tax violations committed by it, and by the extent of damage inflicted on the State budget (public interest). The company refused to acknowledge the unlawful nature of its activity; the company ignored the advice of its official auditor (ZAO PricewaterhouseCoopers Audit), which informed the company's management well in advance of the tax inspection of the illegality of certain operations being used to evade taxes (the promissory notes schemes, royalty-free disposal of property, etc.); the company was actively impeding the government in collecting taxes and penalties prior to and during the enforcement proceedings.

We would also note that the impugned events occurred during the international financial crisis at the end of the 1990s/early 2000s, and the

subsequent recovery of the Russian economy, i.e. when the violations by Yukos were especially harmful to the State budget. The State experienced a period of a transitional economy, which can be attributed to restructuring of the political machinery, assembling and adjustment of legislation, *inter alia*, in the taxation sphere, and reorganization of State bodies.

2.4. Naturally, whatever the wide margin of appreciation granted to a national Government, even in exceptional circumstances, such a margin cannot be boundless. It is always hypothetically possible to imagine certain cases in which the Government's actions would be disproportionate. The question is – who is best placed to assess and stipulate the extent of such appreciation? Clearly, a judge of an international court has less opportunity than a national authority, which is in the thick of the action, to appraise all the nuances and shades thereof, and to establish whether or not certain actions by the public authorities in specific circumstances were reasonable and proportionate. Finally, we must admit that a decision deemed inaccurate today might be reappraised at a later stage. An unambiguously correct appraisal, especially in complicated circumstances, is hardly possible. The multidimensional nature of the various elements involved, specific national conditions, and other circumstances that demand that a national government be granted a margin of appreciation do not deprive the ECHR of its capability to assess the boundaries of such discretion in the light of the requirements of the Convention.

2.5. The presumption that the State[8] is acting in good faith.

The ECHR's case-law relies not only upon a margin of appreciation, granted to public authorities, but also upon the presumption of *bona fides* on the part of a State. As with most other presumptions, the above presumption is rebuttable. However, the standard of proof to overcome the presumption of *bona fides* of a State Government is high, and irrefutable evidence must be adduced (see *Khodorkovskiy v. Russia*, no. 5829/04, § 255-256, 31 May 2011, not final). In the case at hand the Court, in spite of the claims by Yukos, found no reasonable legal grounds to overcome a presumption of the Government's good faith. Moreover, as mentioned above (paragraph 2.3.), the Court did not find any alleged political motive or any intention to liquidate the company or reallocate its assets to the interest of the third parties, or discriminatory actions, as alleged by the applicant.

The Government may act *bona fides*, enjoying a wide margin of appreciation in selecting various means for protecting the public interest; however, the reverse must also be true. The main criterion in assessing the Government's activity as regards compliance with the Convention, alongside the criteria of lawfulness in actions for the public interest, is the

[8] Rectified on 17 January 2012: "*good faith"* was deleted.

proportionality test. Clearly, given the variety and diversity of legal solutions and national systems, defining common criteria for the concept of proportionality is hardly possible. Nonetheless, the ECHR has developed some common approaches.

2.6. Proportionality of the actions employed by the State to secure public interest

A selected remedy might be acknowledged to be disproportionate in cases when it is obviously unreasonable (see *Gasus Dosier- und Fordertechnik Gmbh* (cited above) and other cases). It is worth noting that the above-mentioned test by the ECHR does not include every form of unreasonableness, but only explicit, obvious, doubtless forms. Doubts as to reasonableness can arise on any ground, including the existence of those doubts themselves. We believe that the wider the margin of appreciation granted to the Government, the more evident the unreasonableness should be.

2.7. The ECHR's case-law also takes account of other factors in assessing proportionality. Thus, the existence of an effective and accessible system for appealing against the Government's acts before the courts is of great importance (see *Immobiliare Saffi v. Italy* [GC], no. 22774/93, § 54, ECHR 1999-V). Furthermore, the ECHR examines the availability to a State of less harmful remedies; however, the existence of alternative measures and their non-application in a particular case is not a sufficient and substantive ground to hold the interference in an applicant's private sphere unjustified (see *James and Others* (cited above) § 51, *Borzhonov v. Russia*, no. 18274/04, § 61, 22 January 2009).

2.8. The provision of compensation is a significant criterion in establishing the proportionality of specific measures by a Government. The payment of fair compensation by a State leads, as a general rule, to a finding that the requirement of proportionality has been met. The ECHR tends to apply different approaches to the consideration of proportionality in the case of State interference, depending on whether or not the applicant's conduct was lawful and whether or not the latter behaved in good faith.

In the event of lawful conduct by the applicant, the compensation should, as a general rule, be equal to the damage suffered for the proportionality test to be met. At the same time, even in the event of lawful conduct by the applicant, the compensation may be less than the harm sustained by a private person (see *Jahn and Others v. Germany* [GC], nos. 46720/99, 72203/01 and 72552/01, § 94, ECHR 2005-VI, *Kozacıoğlu v. Turkey* [GC], no. 2334/03, § 64, 19 February 2009, *Broniowski v. Poland* [GC], no. 31443/96, §§ 182, 186, ECHR 2004-V), or compensation might not be paid at all (see *The Holy Monasteries v. Greece*, 9 December 1994, Series A no.

301-A). In other words, in certain exceptional circumstances the State, acting in the public interest, is justified in inflicting greater loss than may seem necessary on a private person who has behaved lawfully and in good faith.

Where the applicant has behaved unlawfully and in bad faith the ECHR accepted a much higher scale of loss, and no compensation at all might be awarded. In respect of tax violations the Court recognizes and advocates the right of the Contracting States to inflict high penalties, especially if the applicant behaved *mala fides* (see *Bendenoun v. France*, 24 February 1994, §§ 33, 46, Series A no. 284). Where the applicant's conduct is criminal in nature, the ECHR accepts confiscation as an indispensable and effective measure against committal of a crime, i.e. an interference in private property interests which implies no payment of compensation at all (see *Phillips v. the United Kingdom*, no. 41087/98, ECHR 2001-VII and *Denisova and Moiseyeva v. Russia*, no. 16903/03, § 58, 1 April 2010).

This approach is partially supported by the concept of justifiable defence, recognised by most legal systems. As a general rule, the damage sustained by the offender may be slightly higher than the damage prevented. However, in certain exceptional circumstances, subject to the provisions of both civil and criminal law, the infliction of damage (harm) on the offender might be held to be lawful, even if the scope of the damage thus inflicted significantly exceeds the actual damage that might have been sustained were the offender to have completed his actions. In other words, in the event of unlawful conduct an offender accepts the risk of possible infliction of damage (harm).

Under this logic, we believe that the infliction of damage on a bad-faith offender, in respect of the levying of taxes owed and imposition of penalties by the national government, does not constitute a violation of the Convention in this regard. In other words, the offender may suffer certain negative consequences, including, *inter alia*, those that he might not have foreseen at the moment of the unlawful conduct and others which are additional to the impact he intended to avoid or escape (arrears, default interest rate, penalties and fines, and other adverse consequences that could reasonably be foreseen under the applicable law). The existence of even highly significant damage in such a case does not in itself mean that the proportionality test has not been met.

2.9. Let us look again at the factual circumstances of this case, this time through the prism of proportionality.

The Court did not detect any violation of national legislation in the measures applied by the Government to the company within the enforcement proceedings. Nevertheless, according to the Court, the manner in which these measures were applied – so to say, "excessively harshly" – does not meet the Convention requirement of proportionality. We believe

that the Court, in finding disproportionality, substantially deviated from the practice developed in the ECHR's case-law. Indeed, the judgment states that, in themselves, the measures applied by the Government were not evidently unreasonable (see, for example, § 654 of the judgment). Moreover, the overwhelming majority of decisions rendered by the enforcement bodies were subject to court supervision, on the applicant's initiative. In some instances those claims were resolved in favour of the applicant.

As to the existence of alternative measures, as was mentioned above, this factor is not decisive. According to the case-file, and the judgment itself, it is not clear whether any other effective remedies existed and whether their adoption would have led to the goal of collecting taxes and penalties, in satisfaction of the public interest. Thus, after the disposal of OAO YNG stocks the funds raised were still insufficient to settle the tax and penalties debt owed to the State budget. The reacquisition (redemption) price was assessed by an independent international appraiser (Dresdner Kleinwort Wasserstein, the investment branch of Dresdner Bank AG), and on the basis of the auction itself. As noted by the Court, before the enforcement proceedings were initiated, the company was probably in a state of pre-insolvency (§ 649), which is proved, particularly, by the fact that the company informed the US Bankruptcy Court of its intention to file a voluntary petition for bankruptcy long before the auction (§ 252). It appears from the case-file that a certain amount of assets was being rapidly transferred abroad. In such circumstances it cannot be ruled out that further procrastination and/or a decision to seize less liquid assets would have significantly reduced the Government's chances of obtaining payment of the taxes and penalties. The only possible alternative, which was offered by the company itself, was to dispose of OAO Sibneft stocks instead of the stocks in OAO YNG. However, the ownership of OAO Sibneft stocks was subject to litigation, and they were consequently regarded as less liquid.

It follows that the decision to seize the applicant's primary business asset and the speed of the enforcement proceedings to collect tax payments do not seem clearly unreasonable. The measures applied by the enforcement bodies were to a large extent determined by the company's actions. The Court recognises the right of national governments to adopt remedies which might grant the State certain privileges over the remaining creditors (see *Gasus Dosier und Fordertechnik GmbH* (cited above)), i.e. the right to apply exceptional measures.

Let us now turn in more detail to some of the elements of the enforcement procedure. As mentioned above, each of such elements does not appear, in the circumstances of the case, entirely unreasonable, and therefore overall the procedure cannot be said to have been disproportionate to the legitimate aim pursued.

2.10. Specific elements of the enforcement procedure/interim measures.

Interim measures intended to ensure enforcement, including putting a lien on assets, may be adopted in good time, before the final decision comes into effect (see *Janosevic v. Sweden*, no. 34619/97, ECHR 2002-VII), provided that such measures will not cause material adverse consequences to interested persons at an early stage and will not substantially affect their defence in forthcoming litigation. In the case at hand, considering the applicant's active impeding of the tax authorities, the use of such interim measure as attachment and freezing orders does not seem unreasonable; the lawfulness of the corresponding State actions was upheld by the national courts. Clearly, interim measures are likely to cause a certain inconvenience in most cases, and might even have adverse consequences for an applicant. However, the applicability of such measures, and the corresponding consequences of their use for Yukos were reasonably foreseeable. The interim measures applied to Yukos did not affect its business activity; nor could they negatively affect the applicant's capability to defend itself in court.

2.11. Seven-percent enforcement fee.

As regards the seven-percent enforcement fee, the Court, having recognised that collection of that fee was a common practice in Russia (see § 647 of the judgment), nonetheless considered the amount to be disproportionate, as it significantly exceeded the expenses which could have possibly been expected to be borne by the State for the enforcement proceedings (§ 655). The Court's reasoning on the compensatory nature of that fee is not fully clear. Indeed, the Constitutional Court in its Judgment № 13-P of 30 July 2001 (§ 485), clearly stated that the enforcement fee is a type of administrative penalty and is not designed for compensation of enforcement expenses. The procedure for such compensation is stipulated in another statutory provision, namely section 82 of the Enforcement Proceedings Act. The penalty in question is imposed by the bailiff should his proposal for voluntary enforcement of the court award not be met (§ 484). Failure to impose the penalty or a reduction in its amount in the case at hand would have amounted to non-compliance by the bailiff with the statutory requirements, and to discrimination against similar non-payers. The Court based its conclusion on this issue on an incorrect interpretation of the national law, having reached its conclusion on the basis of a misunderstanding about the nature and function of the fee in question (compensation, as opposed to a penalty).

2.12. Auctioning of the shares of OAO YNG.

Auctioning of the shares of OAO YNG, one of the key enforcement measures, was not, as stated by the Court entirely (evidently) unreasonable (see § 654 of the judgment), and, therefore, in our view, may not in itself be

seen as disproportionate (see paragraph 2.6. above). In addition, the following events, which took place after the auction was completed, deserve attention, since they might implicitly provide evidence of the actual economic meaning of the enforcement proceedings for the company.

More than a year passed between completion of the enforcement proceedings and the initiation of the bankruptcy proceedings; the bankruptcy proceedings were initiated by a consortium (syndicate) of major western banks, seeking debt collection under a credit agreement awarded by a British court judgment; the management of Yukos repeatedly announced that the auction had not negatively affected the company's commercial viability. It is also worth considering that it was not the business assets of OAO YNG that were disposed of in the auction in question, but a controlling block of stocks. Obviously, such a change in the controlling stockholder might eventually lead to certain changes in the respective company's business. Nevertheless, the respective company's commercial obligations to third parties, particularly OAO YNG's obligations to Yukos, are based on contractual rather than corporate relations (creditors' rather than stockholders' control). Thus, a change in stakeholder (whose opportunity to exercise control over a respective company is limited by law), or even numerous changes in stakeholder, do not automatically lead to a weakening of business commitments. A substitution of the controlling stakeholder is not a legal ground for amendment or termination of commercial contracts, unless the latter explicitly provides otherwise. The case-file does not contain any reliable evidence that OAO YNG breached or failed to perform any of its contractual obligations to Yukos, and the latter made no claims to that effect.

2.13. As a conclusion, with due account for the arguments set out above, and for other circumstances (the applicant's unlawful and bad-faith conduct, the tremendous extent of damage caused by the violations, a lack of consensus among Contracting States, etc.), we believe that the Court, having referred to the concept of a wide margin of appreciation enjoyed by national governments in tax disputes, in fact failed to apply this concept to the case at hand, thus disregarding the ECHR's own case-law.

As to the violation of Article 6 of the Convention

I cannot support my colleagues (hereafter, the Court) in their finding of a violation of Article 6 §§ 1 and 3 (b) of the Convention for the following reasons.

3.1. In the present case dozens of hearings were held in the national courts at various instances and several hundred procedural actions were taken. Of the numerous uncompromising procedural struggles conducted with varying success by the parties, the Court has identified two counts

where, in its opinion, the Government, firstly in the form of the first-instance court, and secondly in the form of the appellate court, acted too speedily. In both instances the applicant was allegedly granted insufficient time to prepare for the court hearings, which had possibly affected the capability of Yukos's legal advisers to counter effectively the tax authorities' lawyers. Both of those episodes concern only the litigation on the collecting of tax payments for 2000. The Court did not find any procedural violations in the chains of court proceedings on collection of tax payments for 2001, 2002 and 2003 or the litigation regarding the enforcements proceedings.

3.2. My first counter-argument refers to both of the omissions identified by the Court.

The ECHR's practice in evaluating tax disputes in the light of Article 6 of the Convention is extremely contradictory, in that, under Article 6, tax disputes do not come under either criminal or civil law (see *Ferrazzini v. Italy* [GC], no. 44759/98, ECHR 2001-VII and *Finkelberg v. Latvia* (dec.), no. 55091/00, 18 October 2001). The ECHR tends to dismiss such cases. An exception is made for cases in which the rigidity of the liability imposed on the applicant verges toward a criminal sanction. At the same time, the rigidity of the sanction is not the sole criterion inviting application of the standards set out in Article 6. A brief overview of the relevant "for and against" practice is set out in the joint partly dissenting opinion of Judges Costa, Cabral Barreto and Mularoni, joined by judge Caflisch, in the case of *Jussila v. Finland* ([GC], no. 73053/01, ECHR 2006-XIII). That particular precedent was referred to by the Court when declaring admissible the applicant's complaint under Article 6 of the Convention (admissibility decision, § 451).

3.3. Nonetheless, in terms of application of Article 6, the present tax case differs substantially from the case of *Jussila*, and from the other precedent which was taken as a basis for the latter, namely *Ezeh and Connors v. the United Kingdom* ([GC], nos. 39665/98 and 40086/98, ECHR 2003-X). In both of those cases the judgments were delivered on the basis of applications from physical persons, not a commercial company. In both Finland and the United Kingdom (and in many other European countries), unlike as in Russia, criminal liability of legal entities is not excluded. Although the Convention's protection extends to the rights of legal entities, one of the four named criteria is qualification of the tax violation as a criminal offence under national legislation. That criterion is not decisive for the purposes of the Convention; however, it must be taken into consideration together with the other criteria.

Under Russian legislation the liability imposed on legal entities is administrative, but not criminal. However, this does not exclude the

possibility of simultaneously imposing criminal sanctions on physical persons – including a company's managers who personally participated in taking an unlawful decision on behalf of a legal entity. It is to physical persons that the guarantees concerning criminal prosecution set out in Article 6 are granted (free assistance of an interpreter, free access to legal representation by a court-appointed lawyer, etc.).

3.4. It should be noted that the judgment in the *Jussila* case was delivered in November 2006, that is, two years after the events and circumstances assessed in the present case. In this respect, given the contradictions and inconsistency in the ECHR's previous case-law, the public authorities hardly had an opportunity to take into account the provisions and standards developed therein. Given the above, in any event, I consider that the standard of requirements with regard to Article 6 of the Convention in this case should have been less harsh.

Let us now examine briefly each of the violations detected by the Court in respect of the litigation concerning payments for 2000.

As regards the lack of time granted to the applicant for familiarization with the case file prior to the hearing before the first-instance court (see §§ 536-541 of the judgment)

3.5. The Court found that the mere four days granted to the applicant for familiarisation with the case files in the tax authorities' ("the Ministry's") premises could have adversely affected the capability of Yukos' numerous legal counsel to prepare the applicant's case efficiently (§§ 540, 551). It is to be recalled that the tax authorities filed the claim with the court on 14 April 2004, and the main court hearing was held more than a month later – from 21 to 26 May 2004 (§ 46). Further to the court's procedural decision of 15 April 2004 the tax authority provided the applicant with an opportunity to familiarise itself with the case files from 17 to 20 May 2004, that is, four days. In the Government's submission, which was not disputed by the applicant, the filed documents primarily contained financial and other detailed source documents, which were formerly in Yukos's possession and/or with which it ought to have been familiar.

With regard to the lack of time granted to the applicant for preparing the case, the Court investigated only one of the numerous elements in such preparation – the time for familiarisation with the case files in the tax authorities' premises. This method of familiarisation is by no means the only one, and, in the present case, was probably far from the primary method for acquiring knowledge of the procedural opponent's arguments and the relevant evidence. Having found the four-day term insufficient for familiarisation with the case files in the tax authorities' premises, the Court

extended this finding to the remaining stages of preparation of the applicant's case. The question is therefore whether the relatively short time (four days) for familiarisation with the case file in the tax authorities' premises could have significantly affected the applicant's awareness of the case files, and whether the applicant was deprived of other available instruments for familiarisation with the case files and of an opportunity to prepare the defence properly? This question must be answered in the negative.

3.6. The ECHR's case-law is based on the presumption that failure to provide documents for familiarisation does not in itself constitute a violation of Article 6. What is required is that the content of a document of which the applicant was unaware at a certain point was material and could therefore have affected the applicant's legal argumentation (see *Krčmář and Others v. the Czech Republic*, no. 35376/97, §§ 40-44, 3 March 2000).

For instance, the ECHR did not find a violation of Article 6 of the Convention in a criminal case in which the text of a sentence transmitted to the appeal court contained significant digressions and discrepancies from the text of the sentence served on the convicted person. All of these differences were held to be insignificant and not to affect - to an extent inconsistent with the guarantees of Article 6 - the applicants' right to defend themselves (see *Karyagin, Matveyev and Korolev v. Russia*, nos. 72839/01, 74124/01 and 15625/02, 28 May 2009)

3.7. I would suggest that, in preparing for the hearing before the first-instance court the applicant was aware, or could have familiarised itself in good time with the content of the documents; the new data which the applicant was allegedly unable to discover from the served documents was not material and could not affect the applicant's legal argumentation.

Thus, the overwhelming majority of the documents with which the applicant intended to familiarise itself initially originated from the applicant itself; the court proceedings were preceded by a long-term tax inspection; the applicant was capable of familiarising itself with the documents in question not only in the tax authorities' premises, but also at the court, since documents are filed simultaneously with the court as attachments to the statement of claim; the tax authorities' arguments with regard to the numerous documents were set out systematically in the tax inspection statement of 29 December 2003 and in the decision (resolution) of 14 April 2004, and remained unchanged throughout the entire court proceedings; the overall duration of the proceedings in the case before all three instances exceeded five months (from 14 April to 17 September 2004); it is not clear from the applicant's subsequent procedural documents how its statement of defence had significantly changed or might have changed had the applicant

been granted more than four days to familiarise itself with the files in the tax authorities' premises at the initial stage of the proceedings.

As to the commencement of the court proceedings before the appellate court before expiry of the time-limit for lodging an appeal (see § 544-548 of the judgment)

3.8. On 1 June 2004 one of the respondents – OOO "Yukos-Moskva" (Yukos-Moskva) – lodged an appeal against the first-instance court's judgment with a court of appeal, as did the tax authority on 2 June 2004. Under a ruling (decision) of 4 June 2004 the hearing was scheduled for 18 June 2004 (see §§ 52-54 of the judgment). On the eve of the hearing, on 17 June 2004, the second respondent – Yukos – also lodged its appeal (§ 55). The court hearing lasted several days, from 18 to 29 June 2004, and the applicant (respondent) was represented by 10 attorneys (§§ 57, 60).

The cassation petition was filed by the respondent – Yukos – on 7 July 2004, i.e. less than 10 days after the appeal court judgment, and long before expiry of the statutory two-month period for applying to the next court instance. The applicant's arguments as set out in the cassation petition were the same as those in its submissions to the appellate court (§ 67). The cassation proceedings were held more than two months later, on 17 September 2004 (§ 70).

The court judgments and decisions at all instances provided a detailed response to the applicant's arguments.

Under the legislation in force at the material time, an appeal had to be judged *within a month* of being lodged with a court, including the time required to prepare for the proceedings and render a decision (§ 423). The judgment on the appeal lodged by Yukos-Moskva on 1 June 2004 was rendered on 29 June 2004, that is, one day before expiry of the statutory one-month term (§ 62).

Yukos-Moskva, which was the first party to submit an appeal, served as a management company for Yukos (§ 1). In those circumstances, it would be unreasonable to assume that these two respondents had not mutually coordinated and adjusted the other's positions or, at the least, were not aware of them, and that Yukos' procedural capacities were less than those of the company acting as the applicant's executive body, namely Yukos-Moskva.

Besides, as noted above, the overall duration of the proceedings in the case at all three instances exceeded five months, the case was subject to review at fourth instance, and the overall duration was nearly fifteen months. It is difficult to accept that the overall duration of the proceedings before the national courts was unreasonably short, and that there was therefore a violation of Article 6 § 1 of the Convention in this respect. I would even suggest that, had the duration of the proceedings before the

appeal court been extended, the applicant would have alleged, so to speak, the opposite violation of the Convention – namely, that the duration was unreasonably long (compare, for example, the allegation of a violation of the Convention with regard to exceeding - by two days - of the time-limit for preparation of the appeal court's judgment (decision, § 43, judgment § 527 (5), and the judges' unanimous opinion that this allegation was ill-founded (§§ 549, 550)).

As mentioned above, the ECHR relies upon the necessity of recognising the supremacy of national courts in ascertaining the facts and circumstances of a given case and interpreting national legislation. The applicant's arguments concerning the lack of time for preparation of its case and the non-observance of the time-limits for examining the proceedings before the court of appeal were investigated by the Court and found to be insufficient and unsubstantiated (§§ 71, 72 and others).

As to the admissibility of the application – Article 35 of the Convention

On 29 January 2009 the Court issued a decision declaring the application admissible. At the same time, under Article 35 § 4 of the Convention, the Court must reject any application which it considers inadmissible due to any deterrent circumstances at any stage of the proceedings, i.e. also after the decision as to the admissibility of the application has been issued. Let us consider a few circumstances which were not fully reflected in the decision as to admissibility, but were in part assessed by the Court.

The power of attorney of the applicant's lawyer Piers Gardner

4.1. The ECHR pays particular attention to verification of the validity of the authority held by the applicant's representative in every case (see, *inter alia*, *Post v. the Netherlands*, no. 21727/08, 20 January 2009), and the absence of a duly-issued authority to act is a ground for finding a case inadmissible. Unfortunately, in the case at hand this requirement was not met.

The case file contains a notice by the insolvency administrator appointed in the course of Yukos's bankruptcy procedure – a private person entitled by law to act on behalf of the company – which revokes the authority to act initially granted to Mr Gardner and empowering him to represent the applicant before the ECHR (see § 299 of the judgment). It was Mr Gardner who filed the documents on behalf of the applicant, both prior to and following liquidation of the company, and who, notwithstanding the cancellation of his authority to act, represented the applicant in the hearings. The notice of the revocation of Mr Gardner's authority was served to the ECHR prior to termination (liquidation) of the company as a legal entity, at a time when executive decisions could be taken only by the insolvency

administrator. In addition, the authority to act granted to Mr Gardner by way of delegation, contained numerous legal omissions, affecting its validity and consequently rendering it null and void, irrespective of the insolvency administrator's notice of revocation, and Professor Valeriy A. Musin, my predecessor as *ad hoc judge* in this case, rightly drew attention to them by dissenting from the majority in the admissibility decision.

As to the admissibility of the case before the ECHR before all domestic remedies have been exhausted – Article 35 § 1 of the Convention

4.2. As was mentioned above, throughout the enforcement proceedings numerous interim measures were taken for the purpose of compelling the applicant to pay the taxes and penalties. Some of these measures were challenged by the applicant in the domestic courts. However, in respect of many other measures the applicant failed to use the available domestic remedies first, but submitted the application in their respect to the ECHR directly (such as the seizure, certain of the bailiff's decisions on imposition of the 7% penalty, etc.).

The Court, irrespective of whether a given measure was assessed by a national court, considered the interim measures in their totality and found that their joint application had been disproportionate (see paragraph 2.1. above). As a general rule, the ECHR may examine any given alleged violation of the Convention only after all domestic remedies have been exhausted. In the case at hand, application of that rule on exhaustion would have led to a requirement to dismiss certain interim measures from the Court's assessment. The absence of certain interim measures from the examined "total" would possibly have mitigated the Court's finding as to the disproportionality of the totality of the interim measures imposed on the applicant in the enforcement proceedings: the "totality" in this case would have been significantly decreased. However, the Court managed to overcome this possible logical trap by stating that, with regard to the considered measures, it was highly probable that the domestic courts would have rejected the applicant's claims, and that applying to them would therefore have been pointless. The Court thereby established an exception from the exhaustibility rule in respect of the examined interim measures (see §§ 636–644 and § 6 of the operative provisions of the judgment).

Meanwhile, in spite of their similarities, such cases contain numerous procedural and factual specificities, which could result in different decisions by the national courts. It is to be noted that the applicant was frequently successful in its procedural struggles with the tax authorities on similar measures. For example, the first-instance court, upholding a motion by Yukos, suspended enforcement of the tax authority's decision on payment of 14 April 2004 (§ 105*)*; the same court reversed a bailiff's decision on imposing a 7% penalty (§ 132) and reversed the bailiff's decision on seizing

the shares (§ 41), etc.; the company repeatedly obtained a reduction in the amounts levied (decision, §§ 42, 53, 66), etc.

In line with the Court's logic, the following - clearly inaccurate - conclusion might be reached. Where there exists an extensive case-law by the national courts on any given matter, any applicant may apply to the ECHR directly, since the outcome of his or her case before the national courts is foreknown with a high, albeit not 100%, degree of probability. Yet a dispute may contain certain specific factual and procedural features, which may lead to the opposite conclusion [by the domestic courts]. Examination and assessment of such specificities is the priority of the national courts.

In view of the above considerations, I cannot agree with the Court's finding as to the exhaustion of domestic remedies.

It is also difficult to refrain from a question concerning the exhaustibility of the measures taken to protect the applicant's interests. Given the national courts' numerous findings as to various violations of the tax legislation, what was to prevent Yukos, its shareholders and other interested parties from claiming compensation directly from those physical persons and legal entities who intentionally took decisions to adopt the abusive tax schemes, resulting in the losses by virtue of their arrogant activity; from those persons who are likely to have enriched themselves as a result of their illicit activity, covered by the Yukos corporate veil.

As to examination by the ECHR of a case which is substantially the same as a matter subject to a procedure of international investigation or settlement

4.3. Under Article 35 § 2 of the Convention the Court shall not deal with any application that is substantially the same as a matter that has already been examined by the ECHR or has already been submitted to another procedure of international investigation or settlement and contains no relevant new information.

In the Court's opinion, the matter accepted for judgment by the Permanent Court of Arbitration in The Hague, pursuant to a legal action by the majority stockholders of Yukos (Yukos Universal Ltd., and others) against the Russian Federation under the Energy Charter Treaty, was not a bar to further examination of the case by the ECHR. The Court considered that, inasmuch as the parties in both cases were not identical the cases were substantially different (see § 526 of the judgment). Such a formal approach in the case at hand can hardly be accepted. In its arguments, the Court refers to a series of benchmarks developed in the ECHR's case-law to distinguish different cases depending on the substantive nature of their respective similarities and divergences (the parties to the dispute, the substance and legal grounds of the redress sought, etc. - § 521). Yet in distinguishing between the cases under examination, the Court applied only the criterion of

the parties to the respective proceedings. In this case, however, that criterion alone is insufficient to conclude that the cases are *substantially* distinct, irrespective of the fact that the legal entities acting as applicants in the two sets of proceedings are not formally identical.

Firstly, a legal entity as a legal institution, that is, as a product of legal techniques, a legal *fiction*, ultimately serves to represent the interests of certain individuals. The use of distinct legal entities in those two sets of proceedings does not itself imply that the judgments in the respective cases will affect the interests of different (distinct) individuals. Bearing in mind the close affiliation of the companies in the Yukos Group, it would be reasonable to assume that, most likely, identical individual persons have a stake in the outcomes in each set of proceedings.

The Court failed to explain why it chose not to observe the rule laid down in the case of *Cereceda Martin and Others v. Spain* (no. 16358/90, Commission decision of 12 October 1992) – the formal identity of the parties in any given case is insignificant when the claim, in essence, is submitted by the same complainants or interested parties.

Secondly, I would suggest that Article 35 § 2 (b) of the Convention, in referring to the substance of the matter, primarily concerns the merits (the substantial part) of the dispute, i.e. those criteria that the Court chose not to consider in the case at hand. Were it otherwise, it would be too simple to overcome the restriction set out in Article 35 § 2 (b) of the Convention by, for example, assigning rights to an affiliate, or submitting identical applications in the name of different stakeholders, etc.

In both sets of proceedings the primary question to be examined by the courts was the same – assessment of the tax schemes applied by Yukos and of the State's corresponding response.