Arbitration Institute of the Stockholm Chamber of Commerce

In an arbitration between

QUASAR DE VALORES SICAV S.A.
ORGOR DE VALORES SICAV S.A.
GBI 9000 SICAV S.A.
ALOS 34 S.L.

Claimants

and

THE RUSSIAN FEDERATION

Respondent

AWARD

20 July 2012

Before the Tribunal comprising:

Charles N. Brower
Toby T. Landau
Jan Paulsson

Representing the Claimants:

Covington & Burling LLP
O. Thomas Johnson, Jr. (until 31 March 2101)
Marney L. Cheek
Jonathan Gimblett
John P. Rupp

Cuatrecasas, Gonçalves Pereira
Jorge Capell Novarro

Representing the Respondent:

Baker Botts LLP
Michael S. Goldberg
Jay L. Alexander
Samuel Cooper
Alejandro Escobar
Jennifer Thornton
Ania Farren

Place of arbitration: Stockholm

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1. GLOSSARY

ADR	American Depository Receipt
BIT	Agreement for Reciprocal Promotion and Protection of Investments between Spain and the USSR, entered into force on 28 November 1991
Hearing	The hearing on the merits conducted from 17 to 25 October 2011
Khodorovsky, Mikhail	Yukos' CEO from May 1996 to November 2003
Menatep	Group Menatep Limited, or GML, at one time the direct or indirect owner of a majority of Yukos' shares
RosInvest	The award on the merits, dated 12 September 2010, in the case of *RosInvest Co UK Ltd v. The Russian Federation*, under the Rules of the Arbitration Institute of the Stockholm Chamber of Commerce
Rosneft	A state-owned Russian oil company
SoC	The Claimants' Statement of Claim dated 20 November 2009
SoD	The Respondent's Statement of Defence dated 4 June 2010

SoRep	The Claimants' Reply Memorial dated 29 October 2010
SoRej	The Respondent's Statement of Rejoinder dated 25 April 2011
T:Day 1:1:1	Transcript of the Hearing, Day 1, page 1, line 1
Tax Ministry	Since mid-2004, renamed the "Federal Tax Service"
Tax Re-Audit (2000)	The Russian Tax Ministry's supervisory audit report dated 29 December 2003 for Yukos' Year 2000 tax filings
YNG	Yuganskneftegaz, the corporate owner of a large Siberian oil field
Yukos	Yukos Oil Company, or OAO Neftyanaya Kompaniya Yukos, formed in 2003 as a combination of YNG and Kuibyshevnefteorgsintez, a refining and petrochemical concern. Producer of about 17% of all Russian crude oil in 2002.
Yukos v. Russia	The judgment dated 20 September 2011 by the European Court of Justice in the *Case of OAO Neftyanaya Kompaniya Yukos v. Russia*

2. INTRODUCTION

1. This document assumes familiarity with the Award on Preliminary Objections of 20 March 2009. In the interest of economy of expression, it will not traverse the procedure and correspondence, which are a matter of record and will be referred to only to the extent significant for the issues resolved in the present Award.

2. The Award on Preliminary Objections upheld jurisdiction with respect to the claims of four of the seven original Claimants insofar as those claims seek a determination of "whether compensation is due by virtue of claims of expropriation raised in this arbitration" under Article 10 of the BIT. (Jurisdiction was not accepted with respect to claims in reliance on Article 5 thereof, which the Claimants unsuccessfully contended had the effect of expanding this Tribunal's jurisdiction through the mechanism of more favourable treatment.)

3. The Claimants complain of the destruction of the value of ADRs equivalent to a certain fraction of ordinary shares in Yukos. At the jurisdictional stage, the Respondent challenged the Claimants' proof of ownership of these ADRs. The Award on Preliminary Objections indicated that the Claimants' proof demonstrated a "form of participation" for the purposes of the BIT, but added that any misrepresentation in this respect would be fraudulent. The Respondent has pursued this matter at the merits stage in light of its latest state of knowledge. This matter is dealt with in Section 6(2).

4. The subsections of Article 10 of the BIT that are relevant for the merits read as follows:

Disputes between one Party and investors of the other Party

1. Any dispute between one Party and an investor of the other Party relating to the amount or method of payment of the compensation due under article 6 of this Agreement, shall be communicated in writing, together with a detailed report by the investor to the Party in whose territory the investment was made. The two shall, as far as possible, endeavour to settle the dispute amicably.

2. [Subsection 2 provides for arbitration in the absence of amicable settlement.]

3. The decisions of the arbitral tribunal shall be based on:

- *The provisions of this Agreement;*

- *The national legislation of the Party in whose territory the investment has been made, including the rules of conflict of laws;*

- *The universally recognized norms and principles of international law.*

5. Article 6 (referred to in subparagraph 1 of Article 10) reads as follows:

Nationalization and Expropriation

Any nationalization, expropriation or any other measure having similar consequences taken by the authorities of either Party against investments made within its territory by investors of the other Party, shall be taken only on the grounds of public use and in accordance with the legislation in force in the

territory. Such measures should on no account be discriminatory. The Party adopting such measures shall pay the investor or his beneficiary adequate compensation, without undue delay and in freely convertible currency.

6. Liability thus requires showing that there has been a type of "measure" contemplated by Article 6 of the BIT which, by way of shorthand, may be described as an "expropriation". This is necessary but not sufficient; it must also be found that "adequate compensation" was not paid. As observed in Paragraphs 41 and 42 of the Award on Preliminary Objections, the Claimants expressly accept that the reference in Article 10 of the BIT to "the amount or method of the compensation due under Article 6" has the effect of excluding the Tribunal's authority to decide whether an expropriation is internationally unlawful under the first three criteria mentioned in Article 6 (public use, conformity with law, non-discrimination). Thus the mission of the present Tribunal is limited to determining the compensation required under Russia's international obligations even under the hypothesis of a lawful expropriation.

7. This case has essentially been debated by reference to documents. There were no witnesses of fact. The Claimants were passive shareholders in Yukos and had no involvement in its activities or in the controversies that underlie this arbitration. The Respondent relies on the acts of its organs. Each side submitted reports from experts who commented on the documentary record, and a number of them were called to testify at the Hearing, namely: for the Claimants Dr Leon Aron, Prof. Jay Westbrook, Prof. Peter Maggs, Mr Sergey Shapovalov, and Prof. Paul Stephen; and for the Respondent Mr Oleg Konnov, Mr Mikhail Rozenberg, and Prof. James Dow.

8. Entire books have been written about the demise of Yukos (e.g. Richard Sakwa, *The Quality of Freedom: Khodorkovsky, Putin, and the Yukos Affair*, Oxford University Press, 2009). The materials submitted by the Parties in this arbitration would easily suffice as research

material for several more. Yet to give an account of every element of the Parties' extensively documented competing narratives would be excessive for present purposes. What is both necessary and sufficient is for the Tribunal to state its views of those elements of the story that the arbitrators consider decisive. Of course the Parties' views of what should be significant will not necessarily coincide with those of the Tribunal.

3. OVERVIEW OF THE CLAIM

9. The Claimants allege that the Respondent unlawfully dispossessed Yukos of its assets and expropriated its shareholders by means of a variety of abuses of executive and judicial power. They affirm that they are owners of Yukos ADRs and demand compensation for their loss. The complaint is put in a nutshell in the first paragraph of the SoC:

> *"They, like all other owners of Yukos, have been the victims of a politically-motivated assault by the Russian Federation, involving the imposition of massive illegitimate tax levies, the seizure and transfer of Yukos' prime asset to Rosneft, a state-owned oil company, and the liquidation of the remainder of Yukos' assets in state-initiated bankruptcy proceedings. On 18 December 2007, Claimants were informed by Deutsche Bank, as depositary, that Yukos had been removed from Russia's company register and that Claimants' ADRs were accordingly now worthless. Today, approximately 75 percent of what used to be Yukos is owned by Rosneft."*

10. The Claimants affirm more particularly (¶ 4) that they:

> *"will show that the massive tax claims brought against Yukos by the Russian Federation for the tax years 2000-04 had no basis in law; that Russia prevented Yukos from paying the tax liabilities in a manner of its choosing so that it could have a pretext to seize Yukos' most valuable asset and to transfer it to Rosneft; and that Russia was responsible both for initiating the bankruptcy proceedings against Yukos and ensuring that they led – via the rejection of a viable restructuring*

proposal advanced by Yukos' management – to the liquidation of the remainder of the company's assets. Claimants will also show that Russia's actions constitute either a direct or an indirect expropriation for which Russia must pay compensation under Article 6 of the Spain-Russia BIT."

4. OVERVIEW OF THE DEFENCE

11. The Respondent asserts that the Claimants are engaged in an abuse of process. In particular (SoRej ¶ 464):

> *"... This arbitration is abusive because it rests on ulterior purposes that were first disclosed during the jurisdictional hearing and that are inconsistent with the Treaty under which this arbitration has been brought. Claimants are not the real parties in interest and have no genuine interest in the arbitration. Claimants have not presented a single party representative. Claimants have not produced a single internal document explaining the rationale behind their original alleged investments or the rationale for initiating this arbitration. Claimants have likely spent more on expert witness fees, alone, than the total amount of their claims. Claimants are not here to vindicate any alleged right of their own. They are nothing more than willing shills in Group Menatep's* "lifetime of litigation." *In this regard, it is worth remembering that the Claimants' counsel has been Group Menatep's lobbyist for years, and the head of its international practice remains a member of Group Menatep Limited's advisory board to this day. Group Menatep, however, is not entitled to invoke the Spain/Soviet bilateral investment treaty. Nor is that treaty intended to be used by Claimants as a tool for harassment."*

12. The Respondent adds (SoRej ¶¶ 467-9) that the Claimants'

> *"... abuse is not, however, that they allegedly purchased ADRs for less than US$ 1 million after the alleged expropriation had begun. Anyone is*

free to speculate on hopes that Yukos would act responsibly, pay its debts with the funds that it had sitting offshore and enjoy a turn of events—all things Yukos did not do. Rather, their abuse is allowing this arbitration to be filed in their names when the only real party-in-interest is Group Menatep Limited, a Gibraltar entity with no rights under the Spain/Soviet bilateral investment treaty.

Claimants, themselves, would never have pursued this arbitration. Quite apart from the absurd disproportion between their own, inflated damages claim and the costs of these proceedings, Claimants concede that six of the "nine measures" on which they base their accusation of expropriation had already occurred ***before*** *they completed their purchases on July 7, 2004, of the ADRs allegedly at issue here. Indeed, by July 7, 2004, Yukos, itself, had warned it would enter bankruptcy if the Russian Federation did not forbear—and the Russian Federation showed no intent of permitting Yukos to get away with its fraud.*

Tribunals, including this one, have recognized that it is inappropriate to act in a manner that aggravates existing disputes. Group Menatep, no doubt, has generated its own dispute with the Russian Federation. Initiating satellite arbitrations for harassment or tactical purposes is an abuse of process. The fact that Rovime was so little involved or concerned that it extinguished itself without even notifying counsel for Claimants is stark evidence of the abuse being perpetrated by Group Menatep here."

13. Even if one were to disregard this abuse and instead consider the merits of the claim, so the Respondent argues, the complaint is a baseless attempt to

overcome the Russian Federation's legitimate application of its tax laws. In particular (SoRej ¶¶ 470-471):

> *"There can be no genuine dispute that Yukos was deliberately engaged in tax fraud. Claimants would have this Tribunal believe that it was entirely acceptable to set up shell companies with no business substance, put them in tax havens, run all of Yukos' profits through those companies, and then abuse the requirement of local investment that justifies the tax haven's existence. Yukos certainly knew better. Its senior executives wrote memos about the high civil and criminal risks they were taking by using the scheme. Claimants knew better too. Such behavior would be no more acceptable in Russia than it would be in Spain or any other country.*
>
> *Yukos was a miscreant. It was the worst of the worst in the late 1990s and, despite a show of transparency, it did not change its spots in the early 2000s. Yukos management repeatedly lied to its auditors at PwC, leading to a termination of the audit relationship and eventually revocation of the audits. Yukos effectively stole from the SocGen Consortium, admitting it could pay the half billion dollars it owed from its European assets, but instead secreting them in Dutch foundations where they could not be reached. Yukos refused the opportunity to reduce the liabilities for its tax fraud by nearly 60 percent, believing it could continue its historic pattern of obfuscation and obstruction. The repeated obstruction of the Russian government's tax enforcement efforts in which Yukos engaged would not be tolerated in any civil society."*

14. The Respondent insists that the Claimants are speculating impermissibly on subjective purposes behind the Russian tax enforcement measures. Quoting from Professor G.C. Christie's often-cited 1962 study on "What

Constitutes a Taking of Property Under International Law," the Respondent writes (SoRej ¶ 473) that:

> *"...this Tribunal must look to the facts, and* "if the facts are such that the reasons actually given are plausible, search for the unexpressed 'real' reasons is chimerical." *This, of course, is right. The Tax Ministry issued extensive findings of tax fraud, which are entirely consistent with the facts and Russian law. The Russian courts reviewed the Tax Ministry's findings and affirmed them in large part, also consistent with Russian law. While it is true that Yukos owed a lot of money, that debt was legally owed and entirely its own responsibility."*

5. *ROSINVEST* AND *YUKOS v. RUSSIA*

15. *RosInvest* was decided on 12 September 2010 by a tribunal presided by Professor Karl-Heinz Böckstiegel and also comprising Lord Steyn and Sir Franklin Berman QC. After a lengthy analysis of the circumstances, they concluded at ¶ 621 that:

> *"[T]he totality of Respondent's measures were structured in such a way to remove Yukos' assets from the control of the company and the individuals associated with Yukos. They must be seen as elements in the cumulative treatment of Yukos for what seems to have been the intended purpose. The Tribunal, in reviewing the various alleged breaches of the IPPA, even if the justification of a certain individual measure might be arguable as an admissible application of the relevant law, considers that this cumulative effect of those various measures taken by Respondent in respect of Yukos is relevant to its decision under the IPPA. An illustration is, as Claimant has pointed out, that despite having used nearly identical tax structures, no other Russian oil company was subjected to the same relentless and inflexible attacks as Yukos. In the view of the Tribunal, they can only be understood as steps under a common denominator in a pattern to destroy Yukos and gain control over its assets."*

16. One year later, the ECHR handed down its judgment in *Yukos v. Russia*, holding broadly – after a similarly lengthy analysis of the circumstances – that in many respects Yukos had failed to substantiate its claims that the Russian Government's tax claims and subsequent liquidation of Yukos were pretextual and discriminatory. On the other hand, the ECHR accepted that Russia had breached Article 6 of the European Convention on Human

Rights in its timing of the Y2000 tax proceedings, and breached Article 1/Protocol 1 with respect to the imposition of penalties and the enforcement proceedings. No damages were awarded; the issue of compensation with respect to the established breaches was held over to a possible subsequent stage of the proceedings.

17. These two very detailed decisions traverse much of the same ground as the voluminous memorials of the Parties in the present case. Yet they come to contrasting conclusions. The result is that elements of each decision are favoured by one of the Parties and criticised by the other.

18. The Claimants argue that *RosInvest's* analysis of the merits is both persuasive and pertinent, and should be given weight as such by the Tribunal. They view *Yukos v. Russia*, on the other hand, as inapposite because it, unlike *RosInvest*, does not involve the same legal standards as an investment-protection treaty. As Mr Johnson put it in oral submissions, the ECHR:

> *"decided whether each of several elements of Russia's behaviour toward Yukos individually violated a provision of the Convention, applying in each case the so-called "wide margin of appreciation" always applied by that court in considering the actions of sovereign governments. It nowhere considered the cumulative effect of Russia's actions towards Yukos, nowhere considered whether those actions violated a typical BIT prohibition against uncompensated expropriation."* (T:Day 1:8:9-17)

19. Mr Gimblett pursued this argument by referring to the ECHR's use of an "extremely lenient standard ... [which] is not applicable in this case", namely the "margin of appreciation" mentioned in the European Convention of Human Rights (Protocol 1, Article 1) and recognised by the Court's jurisprudence (T:Day 1:50:22). Such a "margin of appreciation" is "not found in customary international law", he said, invoking *Siemens v.*

Argentina, ICSID Case No. ARB/02/8 ¶ 354 (2007), and nothing permits "anything approaching the extreme deference applied by the ECHR" (T:Day 1:52:19).

20. Mr Gimblett added that although Protocol 1, Article 1, of the Convention protects individuals from dispossession "except in the public interest and subject to the conditions provided for by law and by the general principles of international law", the ECHR itself, in the *Case of Lithgow and others v. The United Kingdom* 8 July 1986, made clear that:

> *"the general principles of international law ... are not applicable to a taking by a State of the property of its own nationals."* (¶ 112)

21. The grievances of the complainants in *RosInvest* and *Yukos v. Russia* were indeed pursued on the foundation of different legal texts. The proposition that foreigners may invoke a higher standard of protection than nationals does not seem extraordinary, for reasons that may be encapsulated as follows.

22. For one thing, human rights conventions establish minimum standards to which all individuals are entitled irrespective of any act of volition on their part, whereas investment-protection treaties contain undertakings which are explicitly designed to induce foreigners to make investments in reliance upon them. It therefore makes sense that the reliability of an instrument of the latter kind should not be diluted by precisely the same notions of "margins of appreciation" that apply to the former.

23. Moreover, where the value of an investment has been substantially impaired by state action, albeit a bona fide regulation in the public interest, one can see the force in the proposition that investment protection treaties might not allow a host state to place such a high individual burden on a foreign investor to contribute, without the payment of compensation, to the accomplishment of regulatory objectives for the benefit of a national community of which the investor is not a member.

24. This Tribunal is not bound by either *RosInvest*[1] or *Yukos v. Russia*, which arose under different legal instruments than the Treaty which is relevant here. Moreover, the Claimants here had no role in those cases, and have the right that their claims be heard as they chose to present them. Nevertheless, the lengthy texts of those decisions go over much of the same ground that has been covered in this case, and it is natural to examine them in the light of many of the arguments made here as well.

25. The arbitrators understand that the same arguments may be affected not only by differences in the norms articulated in the relevant legal texts, but also by the pleadings and evidence put forward in support of those arguments. Bearing in mind all of these qualifications, the present Tribunal will nevertheless pay respectful heed to the analysis and conclusions of the distinguished arbitrators and judges in these two cases. Indeed they must do so, as both sides in this case have made submissions as to their implications and relative persuasiveness.

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[1] The arbitrators have been informed that the Stockholm District Court issued a judgment on 9 November 2011 to the effect that the *RosInvest* tribunal lacked jurisdiction. That case involves the UK/USSR bilateral treaty. Indeed the present arbitrators, in paragraph 104 of their Award on Preliminary Objections, noted that the two treaties were dissimilar, and declined to comment on *RosInvest*'s conclusion. The judgment was issued by default. Above all, what is of interest here is the possible persuasiveness of *RosInvest* with respect to the merits, not its status as a matter of jurisdiction.

6. JURISDICTION *REDUX*

6.1 The requirements of the BIT

26. In closing argument, Mr Alexander contended that "essential criteria to determine whether or not there has been an expropriation are outside of your jurisdiction in this case" (T:Day 9:107:22).

27. It should be recalled that the Award on Preliminary Objections held that the Tribunal has jurisdiction under Article 10 "to decide whether compensation is due by virtue of claims of expropriation raised in this arbitration" (¶ 155).

28. That Award also recalled (at ¶ 65) a familiar passage from Christie's seminal article: "[T]here are certain types of State interference which, from the outset, will be considered expropriation even though not labelled as such. Among these are the appointment of a receiver to liquidate the business or other property." (See Paragraph 14 above.)

29. Mr Alexander's argument, upon analysis, is old wine in new bottles – indeed an attempt to reargue matters which were settled in the Award on Preliminary Objections. At the core of the debate at that stage of the proceedings lay the Respondent's contention that the BIT did not vest authority in this Tribunal to determine whether an expropriation had occurred. It was rejected after lengthy consideration in Section 2.1 of that Award, leading to the following final statement in ¶ 67: "The Claimants have established that the Tribunal has jurisdiction to decide whether compensation is 'due' to them under international law by reason of the conduct of which they complain (and if so in which amount)."

30. The Respondent is of course free to believe that this decision was wrong. What is not open to it, however,

is to come back at the merits stage in these very proceedings to contend that something it now calls "essential criteria" for determining whether there has been an expropriation are beyond the permissible scope of enquiry of the present Tribunal. The approach taken in this respect will be reflected throughout this Award, notably in the introduction to the lengthy Section 7, which contains the essential treatment of individual issues relevant to the determination of the fundamental merits of the Claimants' case under the BIT. Mr Alexander's argument that the Respondent's objections could not be foreclosed since "the gravamen of the Claimants' propositions could not be fully understood on the merits until we hear the merits" (T:Day 7:142:23-24) is correct as far as it goes, but that is not very far at all. It does no more than to say that the Tribunal, once it gets to the merits, has no authority to go beyond the limits of its authority: a tautology. The limits were fixed in the Award on Preliminary Objections, and the arbitrators have no intention of exceeding them.

6.2 The alleged abuse of process

31. As seen in Paragraphs 11 and 12 above, the Respondent has sought to discredit the Claimants by suggesting that they are not the true parties in interest, and that the entire arbitration is an abuse of process. At its core, this argument is a reaction to the Claimants' disclosure that their costs of prosecuting this case are born entirely by another party, namely Menatep, in part in order to establish that portfolio investors in Yukos are able to recover under BITs to which the Russian Federation is a party. A multitude of such potential claimants are, so it seems, waiting in the wings (T:Day 9:213:8-23). In other words, so the Respondent contends, the Claimants have no stake in this claim, and are not *domini litis* in terms of choosing counsel, experts, or other strategic alternatives in the prosecution of these derivate claims.

32. This objection is unpersuasive. The Claimants purchased shares in Yukos (or, in the case of ALOS 34,

stand in the shoes of such a purchaser) and complain about the destruction of their value. They have mandated Covington & Burling to prosecute their claim. They will be the beneficiaries of any award in their favour. Mr Johnson has represented that this claim has been brought to safeguard the specific interests of the immediate Claimants (T:Day 9:211:1-5, 20-24; 212:5-6; 214:5-8), and that the Claimants have no legal obligation to share the proceeds with Menatep, and nothing more than a moral debt of gratitude to consider whether they will voluntarily pass on a proportion of any proceeds in recognition of the costs incurred by Menatep (T:Day 9:210:14-25).

33. The Tribunal does not see any element of abuse in this respect. The Claimants held very small stakes of Yukos which would scarcely have warranted the commitment of substantial resources to bring international proceedings against the Russian Federation. But there is no reason of principle why they were not entitled to pursue rights available to them under the BIT, and to accept the assistance of a third party, whose motives are irrelevant as between the disputants in this case. Ultimately, the Respondent's complaint, in the event its liability is established, can hardly be raised against the Good Samaritan, but rather against its own officials who acted in such a way as to give rise to that liability.

34. The Respondent raises an associated argument having to do with the alleged spectre of double recovery. The Respondent appears to be concerned about statements emanating from Menatep to the effect that monies it recovers from the Russian Federation, e.g. as a result of proceedings before the European Court of Human Rights or in other arbitrations, will be distributed to injured shareholders such as the Claimants here. The Tribunal does not share those professed worries. It has seen no evidence that the Claimants have some contingent entitlement to share in other cases than this arbitration. To the extent that somehow these Claimants were to receive compensation elsewhere for the harm of which

they complain here, any award in this case could doubtless be resisted by way of some form of set-off.

6.3 The standing of ALOS 34

35. Rovime Inversiones Sicav S.A., a Spanish mutual fund, was one of the original Claimants. For reasons which have not given rise to discussion in these proceedings, it was liquidated on 21 May 2010, and its assets distributed. Rovime's claim in this arbitration (its "*crédito litigioso*") was not listed among the assets to be distributed. Rovime's legal demise and the absence of a legal successor in interest has given rise to an objection by the Respondent. The liquidator, D. Emilio Rodríguez Rodríguez, has certified that the reason for the omission of Rovime's claim in the list of assets was that the claim lacked any accounting value, and that, subsequently to the objection raised in these proceedings, it appeared proper to "reaffirm expressly" that Rovime's *crédito litigioso* "had been assigned to the shareholder ALOS 34, the record owner of 99.99% of the shares of the company."

36. ALOS 34 now seeks to replace Rovime in this arbitration, and the Respondent objects.

37. Faced with this challenge, ALOS 34 through its counsel presented a receipt from the *Registro Mercantíl de Madrid* dated 28 October 2011 showing that the liquidator's certification had been duly received by that official registry, and that this was effective to transfer the *crédito litigioso* to ALOS 34. Mr Jésus Mardomingo Cozas, co-counsel for the Claimants and a Spanish lawyer, appeared before the Tribunal and explained that as a matter of Spanish law the steps taken were the proper (and indeed only) way to deal with so-called "supervening assets" (T: Day 8:113:25).

38. The Respondent sought to discredit the purported transfer of the *crédito litigioso* by pointing out that the liquidation of Rovime appeared to have occurred without the Claimants' counsel having been informed thereof, and that the Claimants scrambled to establish the consequences of this development only in reaction to the

happenstance that the SCC Institute requested formal proof of a power of attorney which Rovime, having been liquidated, could no longer supply. This may well be so as a factual matter. Rovime's investment in Yukos, dating back to 19 December 2003, had not amounted to much more than US$ 100,000. It was the smallest among all the Claimants. It seems likely that the investors behind ALOS 34, as the corporate owner of 99.99% of Rovime's shares having become the transferees of Rovime assets upon the latter's liquidation, were not greatly attentive to the *crédito litigioso* in this arbitration. If so, that is of no moment to the Tribunal here; the issue of standing is a matter of legal formality, and does not depend on the subjective eagerness with which one of a group of claimants participates in the case. The Tribunal is not persuaded by Respondent's contention that ALOS 34's participation in this case cannot be accepted because of its lack of true involvement (as it has effectively ceded control of the prosecution of its claim to Menatep's lawyers) and it is therefore not a bona fide claimant; whether Menatep is keener than anyone else to see findings of liability in this case does not affect the proposition that ALOS 34's rights are to be examined as such. This point has effectively been disposed of in Section 6(B) above.

39. But the Respondent has other complaints as well. It contends, relying on an opinion letter from a Spanish lawyer, Mr Clifford Hendel, that the deed filed with the *Registro Mercantil* has no legal force under Spanish law: "It purports to restate the May 21 assignment but it is undisputed that no assignment occurred that day. Spanish law does not allow for a restatement of legal acts that have never occurred in the first place" (T:Day 8:10:9-13). Moreover, ALOS 34 was not the sole shareholder of Rovime. And Russia cannot be held under the BIT to have agreed to arbitrate with ALOS 34. Indeed, absent the Respondent's consent there is no basis for ALOS 34 to join the arbitration at this stage. Rovime was dissolved by means of an individualised liquidation, not a universal succession, and as a matter of Swedish law – as set out in an opinion letter by Mr Jesper Tiberg, a Swedish lawyer

who the Claimants say, without contradiction, acts for the Respondent in court proceedings in Stockholm – the better view is that in such circumstances (a) there is good reason, notwithstanding a contrary obiter dictum of the Swedish Supreme Court, that consent should be required, and (ii) even if consent is held not to be required as a general proposition it should nevertheless be required under "special circumstances" which are extant here.

40. In answer to the points raised in the preceding paragraph, the Tribunal begins by accepting Mr Gimblett's response to the effect that, in essence, "Rovime has merged into its owner", which he represented to be a "family owned investment vehicle" (T:Day 9:215:6-7). As for the registration of the public deed by the liquidator, purporting to effect the assignment of the claim in this arbitration to ALOS 34, from the documents presented to it (assumed to be genuine), the Tribunal is satisfied that this has been achieved; Mr Hendel's explanations are not apposite to counter this simple conclusion. Furthermore, the Tribunal is not impressed by the contention that the fact that a single share of Rovime's stock, out of 2.7 million shares, did not become the property of ALOS 34 (but was rather assigned to a bank custodian) means that this was not a universal succession. In sum, the Tribunal considers that (a) it was a universal succession, (b) if this was not so, ALOS 34 under these circumstances could nonetheless, given its legal title to the *crédito litigioso*, assume Rovime's position irrespective of consent by the Respondent, (c) there are no special circumstances that cut the other way; to the contrary, (d) ALOS 34 qualifies under the BIT just as Rovime did.

7. INDIVIDUAL MERITS ISSUES

41. The Claimants insist emphatically that their success in this case does not depend upon a showing that the laws of the Russian Federation did not permit the Respondent to treat Yukos as it did. Although the Claimants do argue that the Respondent was not allowed under its own law to carry out the measures by which Yukos was eventually dismantled, as Mr Johnson put it: "The central question instead is: why would Russia treat Yukos as it did if its only interest was the bona fide assessment and collection of taxes?" (T:Day 1:6:17-19).

42. This point serves to underscore the difference between the present case and *Yukos v. Russia*, where the ECHR resolved a series of contentions about Russia's compliance or otherwise with specific provisions of the European Convention on Human Rights, without considering whether or not the Respondent's measures, as a whole, amounted to an uncompensated expropriation of foreign investments as forbidden by this BIT and most – if not all – other BITs.

43. There is thus a fundamental difference between this case and *Yukos v. Russia* notwithstanding that both consider in very considerable detail the narrative of Yukos' demise. But the same can also be said about this case and *RosInvest*, because the tribunal in the latter award held that there had been an *unlawful* expropriation, which as the Claimants here concede is an issue which the present Tribunal is not authorised to resolve under the BIT which is relevant here.

44. This award decides whether there has been an uncompensated expropriation of the Claimants' investment. Any such finding requires a characterisation of the Respondent's conduct, and its effects, as falling within the scope of Article 6 of the BIT (as opposed to

simply the routine exercise of regulatory powers, as per the Respondent's case). For the purposes of this enquiry, the Tribunal will consider the arguments raised by the Parties as so many elements to be taken into account before making an overall assessment. No individual feature of the narrative is necessarily decisive, either as proof of compliance or otherwise with the law, or as evidence of an expropriatory effect as a matter of fact. Indeed, it may not be necessary to come to a firm view as to all discrete contentions if the totality of the circumstances point in a firm direction.

45. It should be clearly understood that the Claimants, while conceding that they may not seek a finding of unlawful expropriation, have never abandoned the position that expropriation may be either direct or indirect – either *de jure* or *de facto*. Indirect expropriation, of course, does not speak its name. It must be deduced from a pattern of conduct, observing its conception, implementation, and effects as such, even if the intention to expropriate is disavowed at every step. The fact that individual measures appear not to be well founded in law, or to be discriminatory, or otherwise to lack bona fides, may be important elements of a finding that there has been the equivalent of an indirect expropriation, an expropriation *by other means*, even though there be no need to determine whether the expropriation was unlawful. Of course much overlap is likely, and that is why the interrogations by the arbitrators in this case are likely to echo those of *RosInvest*. Indeed in many situations it may appear to be a distinction without a difference, to use a phrase that comes to mind when different analytical frameworks seem unlikely to yield appreciably different results, but the conceptual approach is not the same and it is right, in reviewing the Parties' many disputed contentions, to recall that a critical examination of whether the *appearance* of a non-expropriatory measure in fact covers an expropriatory *effect* is not the same thing as deciding whether an expropriation is unlawful per se.

7.1 Were the tax levies on Yukos beginning in December 2003 arbitrary or discriminatory?

46. From December 2003, six weeks after the arrest of Mikhail Khodorovsky, the Ministry of Taxation began a series of re-audits of Yukos' tax years 2000-1, which concluded that Yukos had unlawfully underreported income by routing it through low-tax regions of the Russian Federation. The Claimants assert that these audits were extraordinary, coming less than eight months after an audit of fiscal years 2000 and 2001 in which no criticism had been raised with respect to Yukos' tax "optimization strategy" – and were motivated by the Government's desire to assert dominance over Yukos and its managers. The finding of vast tax liabilities, they say, was based on a specially created legal theory.

47. The Claimants describe the relevant sequence of events as follows (SoC ¶ 28):

"28 April 2003	*Audit of 2000-01 tax years finds that Yukos has a small additional tax liability for those years, unrelated to its use of trading companies in low-tax regions to reduce its tax burden. Yukos pays this liability in full.*
19 September 2003	*Tax Ministry certifies that Yukos, "as of 01.09.2003, has no unsettled liabilities on taxes and other compulsory payments and no violations of the tax legislation"*
23 October 2003	*Tax Ministry recertifies Yukos' compliance with tax laws.*

25 October 2003	*Mikhail Khodorkovsky arrested by FSB agents.*
17 November 2003	*Tax Ministry recertifies Yukos' compliance with tax laws.*
8 December 2003	*Extraordinary re-audit of 2000 tax year begins.*
29 December 2003	*Audit report finds that Yukos owes an additional 99.4 billion roubles ($3.5 billion) for 2000.*
14 April 2004	*Tax Ministry issues Resolution No. 14-3-05/1609-1 (the "2000 Resolution"), demanding payment of 99.4 billion roubles by 16 April 2004.*
15 April 2004	*Tax Ministry petitions Moscow Arbitrazh Court for recovery of 99.4 billion roubles from Yukos. Moscow Arbitrazh Court issues ex parte order imposing wide-ranging asset freeze.*
26 May 2004	*Moscow Arbitrazh Court issues ruling upholding 99 percent of the Tax Ministry's claim.*
29 June 2004	*Yukos' appeal is denied by Moscow Arbitrazh Appeals Court which upholds 100 percent of Tax Ministry claim.*
30 June 2004	*Moscow Arbitrazh Court issues a writ of execution*

permitting the Tax Ministry to enforce the judgment for 2000 against Yukos' assets."

"...Yukos had already paid $1.2 billion in taxes for the 2000 tax year. When that was added to the $3.5 billion tax levy generated by the extraordinary audit, Yukos' total tax burden of $4.7 billion was only slightly less than the company's before-tax income for the year of $4.9 billion.

The Tax Ministry was to rely on the same theories of liability for a series of further tax levies covering the years 2001-04 served on Yukos in the succeeding months. By the time the Tax Ministry issued the last of these demands, Yukos faced a bill of more than $24 billion. To put this tax assessment in perspective, Yukos' net income for the entire period of 2000 through the third quarter of 2003 was approximately $13 billion."

48. The questions that arise for the present Tribunal concern the bona fides of measures taken by the Respondent. Were these actions taken as part of the ordinary process of assessing and collecting taxes, or were they part of an expropriatory pattern? All taxation of course has the effect of a taking of the taxpayer's money; but it is nonsense to say that it is therefore compensable. The tax is the payment of a debt established by law in favour of the public treasury ("the price we pay for civilization", in Holmes's famous expression). But if the ostensible collection of taxes is determined to be part of a set of measures designed to effect a dispossession outside the normative constraints and practices of the taxing powers, those measures are expropriatory and fall within Article 6 of the BIT. And it is then for the Tribunal to consider whether such expropriation has been properly compensated.

(A) The December 2003 re-audit

49. The regular audit of Y2000 had been completed less than seven months before; no questions had been raised as to Yukos' tax optimisation strategy by the use of intermediary affiliates, including trading companies in low-tax jurisdictions. There were three reasons why, in the Claimants' submission, this could not have been a normal supervisory audit:

(i) By early 2002, reports of regional tax audits show that the tax inspectors knew the levels of investment and tax benefits in the trading companies, and of those companies' connection with Yukos;

(ii) Yukos had disclosed the extent of its tax savings by use of low-tax jurisdiction vehicles;

(iii) The new audit resulted in a report which exceeded 100 pages in length within three weeks (29 December 2009).

50. If the theories developed by the Tax Ministry to defend the way Yukos was ultimately treated were correct, the Claimants ask rhetorically, how can it be that the 2002 regular audits of the trading entities did not result in claims, or that the 2003 regular audits of Yukos did not have such an outcome either?

51. The ECHR did not accept Yukos' argument that the Tax Ministry knew of the tax-optimisation "arrangement in its entirety on the sole basis o[f] ... tax declarations and Requests for tax refunds," *Yukos v. Russia* ¶ 592. Whatever the merits of that conclusion, the Claimants in this case do not rely on declarations and refund applications as the "sole basis" for the proposition that Yukos' practice was known to the tax authorities. To the contrary, the Claimants rely on the Ministry's own reports of prior audits, involving both Yukos and some of its more important intermediary trading companies, as

well as on Yukos' public disclosure in 2002 of its tax savings. It therefore seems more pertinent to quote the *RosInvest* Award, the arbitrators in that case having found it "unpersuasive that, for one of the largest and most important companies in Russia, frequently discussed in the media, the tax authorities nevertheless were not aware or at least could not have informed themselves" (¶ 451) and furthermore having found no "convincing evidence that the three week re-audit, or actually other audits, discovered new facts ...." (in ¶ 494).

52. In conclusion, and having carefully considered all the evidence in this case, the Tribunal is unconvinced by the Respondent's arguments to the effect that it neither knew nor could easily have determined Yukos' tax optimisation strategy, or its use of trading companies in low-tax jurisdictions, at the latest by April 2003, in the course of the "regular" Yukos audit. It is notable that the Respondent, while suggesting that the regular audit might have been less thorough than the re-audit (an unsurprising contention in and of itself), has never argued that the earlier audits were marred by any collusion or other improprieties.

(B) The purported legal basis of the revocation of the tax benefits

53. The preponderance of Yukos' tax benefits were granted by the Republic of Mordovia under a law (Law of the Republic of Mordovia on Conditions of Efficient Use of the Social and Economic Potential of the Republic of Mordovia) which gave broad authority to that region. In particular, Article 4, subparagraph 1 of this law established that decisions regarding "application of the taxation regime envisaged in this Law to specific entities shall be made by the Republic of Mordovia", and that Mordovian authorities were also empowered to identify the documentation to be furnished by applicants, to "supervise compliance", to determine the "special taxation regime" for a given entity, to define the procedure for obtaining tax concessions, and to set out the requisite record-keeping by tax-paying entities.

54. Yukos obtained Mordovian tax concessions. It set up trading entities in Mordovia which never, as far as the record shows, fell short of the requirements of the Law under which the benefits were granted. Yet the Respondent treated Yukos as a tax delinquent for having violated an alleged rule of "good faith" in that its tax benefits were "disproportionate" to the investments it had made in Mordovia – notwithstanding that Mordovia was explicitly entitled under the Law to "supervise compliance", and had not seen fit to require any particular level of investment.

55. The ECHR considered that the Respondent's stance in this respect passed muster under the Court's view of the "margin of appreciation", explaining at ¶ 598 that many laws are perforce "vague" and require "judicial interpretation" to be developed as "questions of practice". This reasoning does not really meet the argument made by the Claimants in this case to the effect that it is simply wrong for a citizen to be sanctioned for bad faith when he has acted in accordance with the rules established by authorities having explicit statutory authority to supervise the relevant conduct, and without any criticism by those authorities.

56. The Respondent's position is further weakened by the fact that it cannot point to a precedent where the putative proportionality rule had been invoked against a similarly situated taxpayer. In the absence of a sound and proven legal doctrine to justify itself, it is no answer for the Respondent to say that the regional tax incentive system had been shown to result in an unacceptable loss of aggregate State revenues, and that the correction must start with someone. The self-evident correction in a legal regime which is revealed not to contain adequate constraints is to re-conceive and re-calibrate those limits, and to enact revisions by legislative amendment, not by ad hoc administrative determinations based on a nearly infinitely open-textured notion like that of "good faith".

57. Indeed an article published by Vladimir Samoylenko in April 2004 ("Government Policies in

Regard to Internal Tax Havens in Russia" 34 *Tax Notes International*, 5 April 2004) captured the point very well, demonstrating that the tax authorities were quite aware of the great advantages derived by big business from the special tax regions, and that they were engaged in debates about it. (The Claimants have also submitted evidence of Audit Chamber reports documenting how it was possible to derive substantial benefits from a region despite an insubstantial presence there; see, e.g. the *Audit Chamber Bulletin* No. 3 (75) (2004), "Report on the Results of the Review Concerning Implementation of the Decisions Made by the Collegium of the Audit Chamber of the Russian Federation following the Results of the Audits in Respect of Performance of Audit Activities Ensuring Receipts of the Federal Budget in the Regions of the Russian Federation", looking at the period 2001/02 and concluding at p. 127 that the benefits in Mordovia "amounted to 16.3 times the Federal subsidiaries"; and that in Kalmykia the amount of tax benefits was offset by no more than 5.4% by way of investments of the beneficiaries.) Samoylenko made clear that it was perceived before the year 2000 that the policy was having deleterious effects, and that the obvious remedy – legislative reform – was identified by the Tax Ministry as early as 2001. Some vested interests sought to preserve the system as it was, and therefore the ultimate federal cap on regional benefits did not take effect until January 1st 2004. The following comment by the author is of clear present relevance:

> *"The tax authorities must not lose sight of the fact that the elimination of the regional tax havens is a policy change. A once favoured means of funding local budgets has been rejected. As a matter of fairness, tax authorities should not seek to shift blame for the undesired policy to Russian businesses who took advantage of the policy."*

58. The Respondent did not counter these arguments, in either its opening or closing oral submissions. Samoylenko was entirely absent from its presentations,

save in response to a question from the Tribunal, where a passing reference to Samoylenko was made to the inconsequential effect that one must "distinguish between use and abuse" (T:Day 9:158:15).

59. In its written arguments, the Respondent focused on what it sought to portray as Mr Samoylenko's views on a quite different matter, namely the notion that tax benefits were restricted by a rule of proportionality. This argument backfired, since the Claimants were able to point out that the author never made such a statement, but to the contrary – and repeatedly – observed that the tax haven practice was to offer generous advantages *in return for fixed fees*. Moreoever, the Claimants were quick to point out that the *RosInvest* tribunal flatly rejected the proportionality argument when it was put to the arbitrators there (¶ 450).

60. Looking at the facts of this case, the salient feature is undisputed. Yukos developed the practice of using controlled trading companies as intermediaries for its vast volume of sales. Sometimes these trading companies were arrayed in multiple layers, buying and reselling Yukos' output from other entities of the Yukos group. When the intermediary entities were located in a low-tax region of Russia, they unsurprisingly purchased the goods at a low price and resold them at a higher price, thus generating profits taxed at a low rate. The regions' objective was to attract economic activity; and they were authorised to grant these tax advantages by dispensation from the federal government by reason of their special development needs within the framework of macroeconomic policy. Some regions were thus in a position to grant very substantial advantages. For example, when the Russian Federal profits tax in 2002 stood at a rate of 7.5%, the regional and local profits taxes were 16.5%. One immediately sees that insofar as a region was willing to forego a part – or indeed all – of the 16.5%, this raised a number of issues of public policy within the Russian Federation. For example, if a profitable enterprise moved its tax domicile from region X, which had no authority to grant tax concessions, to

region Y, which was prepared not to tax profits at all (thus contenting itself with prospects of increased employment or the collection of lesser taxes of a different nature) the result would not only be starkly negative for region X, which would lose its tax receipts entirely, but also possibly for the Federation, which might have to come to region X's rescue if this occurred on such a scale as to compromise the region's capacity to finance the maintenance of public services. As for region Y, it might well say that modest revenues are better than none, ignoring that the authority to concede tax advantages had been reserved for relatively unprosperous regions which required Federal subsidies. To put it simply, ill-conceived regional concessions would drain the aggregate public treasury.

61. The Tribunal has seen evidence of tension between the central State and the regions with respect to the authority to legislate and to regulate. Regional overregulation was thought to frustrate State policy (and naturally create opportunity for corruption), while regional laxity with respect to special fiscal regimes could undermine the public treasury. Thus, to take a problem of present relevance, permissive tax domiciliation in a given region, when coupled with low tax rates, might allow schemes having the perverse effect of draining significant tax revenues from one region without increasing them elsewhere, as the low-tax region would be happy to take the 100 thousand it would otherwise not have received without caring that the corporate migration thus deprived the original region of 100 million.

62. One form of similarly unintended consequences might be the failure to disqualify inter-group transfers. This is a well known challenge to modern fiscal policy-makers. A multi-national group of companies which produces goods in a high tax jurisdiction is unlikely to be able to avoid those taxes by a simple inter-group transfer to a subsidiary entity located in a tax haven at a price which reflects nothing but cost, and therefore attracts no income tax. This is the familiar problem of transfer pricing, which is cured by the authority to

challenge the price and to deem the taxpayer's true income to have been higher.

63. The problem within the Russian Federation was similar, but in Yukos' case the approach taken by the Respondent to rectify allegedly unintended windfalls to Yukos was, as it explains, quite different. Instead of simply challenging the transfer prices, with the aim of reallocating proper revenues to the original producing/selling entity so as to reflect an arm's length transaction, the Tax Ministry developed a concept of "abuse of right", with the salient objective of disqualifying sham transactions. In addition – whether as alternative or confirmatory theories is not always clear – the Ministry referred to criteria of "proportionality" of investments to tax savings, and "real ownership".

64. Countless words have been written and spoken in the course of these proceedings about the proper understanding of the position under Russian law. Indeed, the debate has included excursions into the realm of comparative tax law, as the Respondent has sought to demonstrate that many advanced legal systems include the concept of "abuse of law" and the disqualification of sham transactions. The Claimants, for their part, have insisted that the Respondent's treatment of Yukos involved entirely novel and discriminatory legal theories invented for the sole purpose of covering what was and remains fundamentally an unlawful dispossession of private property. In sum, the competing narratives might be described as "sham transactions" vs "sham taxes".

65. Erudite expert reports were furnished by both sides on these issues, and significant time was spent in the course of the hearings in questioning some of their authors. To explore all the ground covered by these arguments and rebuttals, which at times under the direction of skilled cross-examination involved extended excursions at a great distance from the facts of this case, would result in an award of unwarranted length. It should suffice for the Tribunal to set out its core conclusions:

- Since the loss of tax revenues was evidently attributable to non-arms'-length inter-group pricing, the natural correction would be to disqualify those prices and to reintegrate into the producing entity's tax base an amount which would restore arm's length.

- The basis for such a correction of the problem apparently exists under the applicable tax regime, or by virtue of Article 40 of the Russian Tax Code. Even if that were not so, or if there were found to be a failure of safeguards in the terms under which certain regions could grant tax advantages, such matters fall to be addressed by legal reform.

- To characterise behaviour as violating a broad concept of "good faith" when a taxpayer adopts behaviour precisely to take advantage of tax benefits created with the intention of inducing the corresponding conduct seems quite extraordinary. It is hard to see why the taxpayer should be blamed for the generosity of those benefits. Absent proof of collusion with officials charged with administering the tax regime, it is difficult to accept that the taxpayer should be held to a duty to conclude, against the text of the regulations, that the scope of the tax advantage had been defined as broader than what the drafters intended.

66. To counter the observation that what Yukos did was not only not prohibited, but indeed authorised, the Respondent invokes a particular type of breach of good faith, namely that of a "sham" transaction. This concept was explored at length in the course of cross-examinations of expert witnesses, notably of Professor Stephan (called by the Claimants) and Mr Konnov (called by the Respondent). The proposition advanced by the Respondent is that tax authorities may disregard transactions if they have no "reasonable economic or other purpose" other than the securing of a tax benefit. Although the discussion was conducted against a background of impressive familiarity with the relevant legal texts and cases, and occasionally at a very high level of abstraction, in the end the Tribunal can summarise its relevant findings quite simply and succinctly.

67. The Tribunal is unwilling to find that Yukos engaged in sham transactions with its affiliated trading entities. For one thing, the notion of a "sham" suggests something surreptitious, whereas the tax authorities obviously had access to the tax returns of both Yukos and the affiliated entities in question and would, or should, have had little difficulty in seeing that Yukos was assigning significant revenues to the latter by way of inter-company transfers. These transfers might be questioned on the basis of the arm's length standard discussed above, but not as shams. (Incidental internal communications advising staff members not to preserve documents relating to the arrangements are not, in the Tribunal's view, decisive proof of a guilty corporate conscience; they might just as well suggest a disinclination to call attention to the tax savings made, particularly if there were apprehensions of aggressive audits. At any rate, as said, Yukos' intragroup practices were known or could readily have been ascertained.) That leads to the more significant consideration, namely that a sham transaction above all involves an attempted masquerade, attempting to disguise the very nature of what is being done. An excellent example emerged in the form of the so-called *Sibservis* case, Resolution No. 367/96 of 17 September 1996. There the taxpayer

purported to "borrow" money from customers of its goods, and "repay" the "loans" by delivery of the goods. The repayment of loans, as opposed to monies received on account of goods sold, was not subject to VAT. The transaction was recharacterised by the tax authorities. This was indeed dissimulation.

68. In the present case, there was nothing of the sort. The sales transactions were just that: the transfer of title to goods for a certain price. From the ultimate independent purchaser, a legal relationship was created between that purchaser and the intermediary Yukos affiliate. There was no "fake" transaction. The buyer had a right to certain deliveries, the duty to make certain payments, and a right to bring action against the intermediate entity, notably in the form of an international arbitration – but no privity to bring an action against Yukos, with which it had no contractual relations.

69. If one puts to the side the idea of sham transactions, one is left with the question whether a taxpayer should not be allowed to conduct its business by choosing alternative A over alternative B for the sole purpose of deriving a tax benefit. The answer in Russian law, as reflected in point 4 of the Supreme Arbitrazh Court's Resolution No. 53 of 12 October 2006, is – to use the phrase employed by Mr Alexander for the Respondent (T:Day 6:13:5-8) – that "if there are two options, both of which have the same economic substance, the taxpayer is entitled to choose between those options." The true economic substance of Yukos' vast business was to sell into the market to independent purchasers. This could be done directly, or alternatively through affiliates. The second alternative was more attractive, due to the availability of tax benefits precisely designed to stimulate the establishment of business activity in the Russian low-tax jurisdictions. The economic substance of the arrangement was the same; goods produced by Yukos were purchased by an independent buyer at a market price. To insist that Yukos should not be allowed to sell to an affiliate at a below-market price is, once again, something quite different; that has to do with the

prohibition of the terms of a transaction, not a claim that it was bogus.

70. Similarly, the plausible notion that tax benefits must bear some reasonable relationship to the investments made by the taxpayer seems so self-evidently suitable for consideration at the time of creating the low-tax regime that its absence cannot be considered an accident; if in practice the omission seemed an error, the obvious remedy is amendment rather than unpredictable judicial sanctions by reference to an unspecified criterion of "proportionality".

71. The same may be said with respect to the use of intermediary entities which have negligible "economic substance". If that were to be a disqualifying factor, it would surely be a simple matter to make clear that some quantified "substance" is a requirement, rather than to leave it to the happenstance of a subsequent judicial opinion about the matter. In the case of Mordovia, the investment law specifically listed the wholesale trade in fuels and lubricants as the type of activity that would qualify an investor for benefits under the law. Given that no hydrocarbons are produced in Mordovia, it seems quite clear that such a wholesaler might do its business with no physical plant and a very limited staff of traders sitting at their consoles.

72. The ultimate justification, in the eyes of Mr Konnov, turned out to be the taxpayer's "motivation" (T:Day 6:148:11-25), in the sense that improper motivation was evidence of abuse, and therefore a ground on which to disqualify the claimed benefit. Mr Konnov's knowledge of Russian tax law and cases was most impressive, as were his acute perception of nuances in the questions put to him and his clarity in responding to them. This is all the more reason to give weight to the fact that he concluded that it all came down to the distinction illustrated by two simple hypotheses which he referred to repeatedly in his answers before the Tribunal. In the first, Yukos owned no trading companies but decided to hire professional traders and set them up in a new company;

"if they decide to do that in Mordovia, it is true business operations, true trading company, then probably I have no problem with it" (T:Day 6:210:6-9). In the second, "if I have trading corporations in Moscow and I go to Mordovia and I set up a company there, what is my motivation" (T:Day 6:148:14-16).

73. If the taxpayer structures his business with tax minimisation as the "sole or predominant reason", "you have a problem" and "the fact pattern in the Yukos case is pretty easy ...." (T:Day 6:212:1-10).

74. The Tribunal is unpersuaded. In the first place, the analysis here shifts appreciably from the notion of sham transactions and even from that of "no reasonable economic or other purpose" to that of a dominant motive of tax savings. The distinctions are decisive. To recall Mr Alexander's words, "if there are two options, both of which have the same economic substance, the taxpayer is entitled to choose between these options". In other words, the choice is exclusively tax driven. It is difficult to see how it could be otherwise, in a world filled with major corporations openly structuring their businesses through low-tax jurisdictions. The distinction between the hypothesis of a new trading company versus a migrating trading company, positing the former as acceptable and the latter not, is not convincing. In the first hypothesis, the two options are incorporation in a high tax jurisdiction versus incorporation in a low tax jurisdiction. In the second, the choice is between *remaining* in a high-tax jurisdiction versus *migrating* to a low tax jurisdiction. There is no distinction of principle. Business decisions, once made, are not immutable. They are revised in accordance with negative and positive developments, such as increased taxes in the current jurisdiction or tax benefits in a jurisdiction where it is possible and lawful to relocate. The notion of abusive motivation simply does not fit.

(C) The attribution to Yukos of the additional tax associated with income of the trading companies

75. It is one thing to say that Yukos remained the owner of goods which it had purported to sell directly to its affiliates because its contracts with them were a sham, but quite another to insist that the result of repudiating purported sales among entities controlled by Yukos was that *Yukos* somehow became the owner of the goods. This obviously has nothing to do with the proposition that the sales were sham transactions, but rather with the very different notion that Yukos, albeit not a party to the transaction, should be treated as having become the owner. The adoption of this approach by the Respondent obviously made it instantly possible for it to view Yukos itself as a tax debtor by reason of profits which it had not made, and would benefit from only upon the contingent payment of dividends.

76. This move raises obvious legal issues as to how this conclusion might be justified. They were dealt with comprehensively in writing by Professor Viktor Pavlovich Mozolin, notably by reference to the unprecedented way in which the tax authorities used Article 209 of the Civil Code. Professor Mozolin was not called for cross-examination by the Respondent, who chose instead to challenge his opinion by relying on the contrary arguments of Mr Konnov. It would be perverse if insightful expert testimony were to be disregarded simply because the party which disagrees with it chooses not to confront the author. Indeed the Tribunal is inclined to give weight to Professor Mozolin's statement that Article 209 appears in a general part of the Civil Code which gives way to Chapter 14, dealing with the acquisition of property in particular. Mr Konnov in fact accepted that Article 218, which appears precisely in Chapter 14, properly covers a situation such as that of Tomskneft, a Yukos producing company, selling oil to Ratibor, one of the Yukos trading companies (T:Day 6:83:25). Professor Mozolin went on to conclude that the Tax Ministry's unprecedented invocation of Article 209 "to identify

someone other than the title holder as the owner of property is .... illegitimate" (Opinion, ¶ 9).

77. Professor Mozolin is among the most senior of Russian academic figures: head of the Civil and Family Law Department of the Moscow State Academy of Law, and one of the drafters of the Civil Code of the Russian Federation. His expert testimony focussed entirely on two fundamental and over-arching topics, as to which his reasoning stands challenged – but not confronted. As they were both at the heart of the putative legal underpinning of the measures at issue in this case, the decision not to call him to the stand was quite remarkable. As to the first of the two topics, his conclusion is uncompromising: "My frank assessment is that this invocation of Article 209 was absurd" (¶ 6). He explained that "there is no provision of the Civil Code that operates to transfer ownership of the oil to Yukos or declare Yukos as the 'actual owner' of the oil and based on the provisions of Article 209.... I have not encountered the concept of 'actual owner' in my more than 50 years as a legal scholar."

78. Professor Mozolin's second topic was to examine the proposition that there is a distinction between good and bad faith taxpayers, and that the tax authorities therefore are justified in seeking to determine to which category a given taxpayer belongs, and to treat him accordingly. Professor Mozolin had no truck with this concept (nor did the *RosInvest* tribunal, at ¶ 449), and the Claimants did not have to look far to find authority to support the proposition that Russian law gives all persons the benefit of the presumption of good faith, including taxpayers.

79. Reverting to the issue of Article 209, without needing to adopt Professor Mozolin's word *illegitimate*, the present Tribunal contents itself with observing that the tax authorities' reference to Article 209 seems to have been rather cavalier, reaching for the nearest available general legal text – defining the rights of ownership as possession, use, and disposal – for the sake of appearance, without explaining how the assignment of ownership to

Yukos could override the transmission of title, as per the sales contracts, in light of the directly apposite Article 218. Mr Konnov's defence of the tax authorities' approach was that "the tax authorities referred to Article 209 not as a standalone/separate concept but in the context of the anti-abuse theories described above" (2nd witness statement ¶ 43). This comment rather gives the game away; if the reference to Article 209 did not "stand alone", it was unnecessary; if it was unnecessary, why was it invoked, if not as a rather jejune fig leaf? Rather than a part of the foundation of undoing a sham transaction, this seems to be an indicium of a sham tax assessment. (The Tribunal is aware that Article 209 may have been invoked by the Tax Ministry once before Yukos, as a basis for making an assessment, but there had been no judicial endorsement of it until Yukos.)

(D) The rejection of the VAT refund

80. The unattractiveness of the Respondent's position in this connection is readily apparent. The amounts involved were vast – in excess of $13.5 billion. The export sales in question undoubtedly qualified for VAT refunds. The trading company sellers had duly applied for them. But once the tax authorities had invalidated the transactions by which the sellers had come into possession of the goods, they concluded that Yukos was the true original owner and therefore should be deemed to be the true export seller. If this was so, one would expect that by a parity of reasoning under their basic premise, the tax authorities should have held that the true applicant for the refund was also Yukos – and that Yukos was therefore entitled to the VAT credit in the same way as it was assigned the debit for the profit tax. To try to have it both ways would surely bespeak unprincipled hostility towards the taxpayer.

81. Yet that is precisely what the tax officials did – with the subsequent endorsement of the courts.

82. Unsurprisingly, *RosInvest* viewed this conduct in the harsh light it deserves:

> *"The extremely formalistic interpretation of the VAT tax law regarding Yukos and its trading companies to the effect that, though exports were undisputedly not subject to VAT, the documentation also undisputedly submitted by the trading companies could not be used in relation to Yukos and thus Yukos was liable for more than US$ 13.5 billion in VAT related taxes is difficult to accept as a justification for a tax liability the size of which was sufficient to lead Yukos into bankruptcy."* (¶ 452)

The present Tribunal entirely endorses this conclusion, and agrees with the Claimants that the ECHR appears, in ¶¶ 601-602, to have entirely missed the point being made, namely that if the tax authorities were going to attribute to Yukos the transactions carried out in the names of its trading companies, they should also have attributed to Yukos the submission of normal VAT documentation by the trading companies. Given that the export transactions in question were indisputably zero-rated for VAT purposes, the refusal to do so can only seem confiscatory to a degree which comes close to validating the claims in their entirety on this basis alone.

(E) The speedy and robust execution of the judgment enforcing the Y2000 assessment

83. The Claimants observe that Russian law would have given an allowance of three years for the execution of the judgment, and argue that this would plausibly have led to an arrangement for payment without the need to seize and sell off YNG.

84. The effective date of the writ of execution of the Moscow Arbitrazh Court, allowing the Ministry to enforce its $3.5 billion tax claim, was 30 June 2004. The Tax Ministry had up to three years to act on the writ, say the Claimants, but demanded payment within five days. The Ministry ignored a number of proposals from Yukos to pay this amount notwithstanding the freeze on its assets – e.g., by execution against its shareholding in Sibneft.

Instead, on 20 July the Ministry of Justice announced that it would sell YNG, a Yukos asset the Claimants say was worth at least $15 billion, to satisfy the 2000 debt. In a Prospectus dated 14 July 2006, Rosneft was to value its YNG interests at $57.7 billion.

85. The Claimants argue that since the Respondent had put into place a freeze on Yukos' assets and since interest would run on taxes due, it had no legitimate reason not to allow Yukos reasonable time to work out means of payment that would allow the corporate taxpayer to avoid the loss of its largest producing assets, and indeed the ultimate dismantlement of the entire enterprise.

86. The Respondent's counter, to the effect that it might have been exposed to a charge of abuse of right if it tarried in enforcing the tax debt, and allowed interest to accumulate, is feeble indeed. That ostensible worry would have been neutralised, if indeed it was sincere, by asking Yukos to waive any such claim as a condition of reprieve.

7.2 Did the Respondent prevent Yukos from discharging the (disputed) tax debts?

87. The Claimants contend that the Russian Federation prevented Yukos from discharging or settling its tax liabilities so that it could seize YNG and sell it to Rosneft at a bargain price. Yukos specifically takes issue with the 15 April 2004 asset freeze, the Russian authorities' failure to consider Yukos' proposals of alternative means of paying the tax assessments, and the seizure and sale of Yukos' shares in YNG. The Respondent, on the other hand, defends the propriety of its actions.

88. The question that arises for the present Tribunal is whether the 15 April 2004 asset freeze, the Respondent's failure to consider Yukos' proposals of alternative means of paying the tax assessments, and the seizure and sale of Yukos' shares in YNG prevented Yukos from discharging its tax debts. If the answer is in the affirmative, the question arises whether in bringing about this result the Respondent acted in a manner normally to be expected of

a taxing authority truly seeking to collect lawfully levied taxes, or whether instead Respondent's actions were so antithetical to ordinary means of achieving that objective as to indicate that it had another goal in mind. The latter conclusion would support the Claimants' theory that the Russian Federation's goal was to expropriate Yukos, and not legitimately to collect taxes.

(A) The 15 April 2004 asset freeze

89. According to the Claimants, Yukos could have paid the 2000 tax levy of some $3.5 billion and survived as a healthy company, but was prevented from doing so by an order, issued the day after the Tax Ministry's demand, to freeze its assets. The initiative led to the following sequence of events (SoC ¶ 31):

"15 April 2004	*Moscow Arbitrazh Court issues ex parte order imposing wide ranging asset freeze to secure alleged liability of $3.5 billion for 2000.*
16 April 2004	*Deadline for voluntary payment of tax assessment expires.*
22 April 2004	*Yukos petitions Moscow Arbitrazh Court protesting the freeze as unlawfully disproportional and requests that the court instead freeze Sibneft shares held by Yukos worth more than the $3.5 billion claim.*
23 April 2004	*Moscow Arbitrazh Court denies Yukos' request.*
17 May 2004	*Yukos appeals the Moscow Arbitrazh Court's decision.*
2 July 2004	*Yukos' appeal to the Moscow Arbitrazh Court of Appeal is rejected."*

90. The Russian Federation allegedly made it impossible for Yukos of its own accord to discharge the liabilities imposed on it by the Tax Ministry: "the only way for Yukos to discharge its tax liabilities in full was to sell or borrow against assets that were subject to the 15 April 2004 asset freeze." (SoRep ¶ 289.) But, as recounted below in Section 7.2(B), Yukos' repeated requests to do so were purportedly ignored by the bailiffs.

91. The Claimants contend that "[i]f the scope of the asset freeze was genuinely within the discretion of the Tax Ministry and Moscow Arbitrazh Court, the decision to exercise that discretion in such a disproportionate manner was arbitrary in nature and expropriatory in effect." (SoC ¶ 140.)

92. The Respondent answers that the asset freeze did not prevent Yukos from discharging its tax liabilities; rather, Yukos simply did not want to pay. (SoRej ¶ 226.) The Respondent suggests, contrary to the Claimants' contention, that the asset freeze did not cover the "assets or activities" of Yukos' subsidiaries or affiliates; did not affect Yukos' principal activity of the production, processing, and sale of oil; and did not preclude Yukos from selling non-Russian assets. (SoRep ¶¶ 285-87, SoRej ¶ 227.) The Respondent also points to comments made by Yukos' management and representatives that the 15 April 2004 asset freeze did not have a significant effect on the company's operations. (SoRej ¶ 224.)

93. The Respondent further pleads that the asset freeze was a reasonable response to the risk that Yukos would further evade its fiscal obligations:

> *"The motion for injunction by the tax authorities was reasonable and justified when it is considered the amounts at stake, the clear indications by YUKOS' management that YUKOS would not settle its tax liability voluntarily, the decision of the tax authorities to take a more conservative approach with respect to enforcement of 2000 tax arrears and interest through court proceedings, a[s] well as the*

prior history of YUKOS' tax evasion." (Konnov First Report, ¶ 180.)

94. The Tribunal observes that the lawfulness of the asset freeze was reviewed and confirmed by the Russian courts, as noted by the ECHR. (*Yukos v Russia*, ¶ 641.) While the Tribunal is mindful that it is not an appellate body to scrutinize the decisions of domestic courts, the Tribunal notes that it is not bound to accept such decisions to the extent that they sanction "actions [that] breached international law by depriving the claimants of adequate compensation for the dispossession of which they complain." (Award on Preliminary Objections, ¶ 45(ii.))

95. The Tribunal is of the view that the asset freeze did not by itself "breach[] international law by depriving the claimants of adequate compensation for the dispossession of which they complain." The Tribunal therefore will not scrutinize and opine upon the decisions of the Russian courts upholding the asset freeze. But, as discussed below, the Tribunal finds that the timing and comprehensive scope of the asset freeze were among several factors that substantially contributed to preventing Yukos from paying its tax debts.

96. The timing of the asset freeze must be viewed in context, against the backdrop of the Tax Ministry's demand for $3.5 billion in back taxes. The *ex parte* freeze on Yukos' assets took place on 15 April 2004, when *the day before* the Tax Ministry had demanded $3.5 billion in taxes and *the day after* had been set as the deadline for voluntary payment. The timing of the asset freeze undoubtedly was a hindrance to Yukos in accomplishing the already vast task of paying the alleged $3.5 billion tax debt within two days.

97. The difficulties associated with this extremely short deadline were compounded by the fact that the Russian Federation froze substantially all of Yukos' non-cash assets. The Respondent argues that the asset freeze did not cover the "assets or activities" of Yukos' subsidiaries and, therefore, Yukos could have caused its subsidiaries to sell off their assets and pay the proceeds as

dividends to Yukos. It is, however, implausible to contemplate that the Russian authorities would have allowed the value of the very assets that were frozen to be diluted in this fashion. The Tribunal is also sceptical of the relevance of the comments by Yukos' management and representatives that the 15 April 2004 asset freeze did not have a significant effect on the company's operations. For Yukos to say at that point that its "operations" would not be affected would be understood by the average business executive to mean exactly that: the search for, exploitation, extraction and sale of petroleum products remain unhindered and will continue. Normal business is not interrupted by a freeze on non-cash assets. Even were such "statements against interest," as Respondent characterizes them, construed more broadly, however, they must be considered as of the time they were made, in April, May and July 2004 before certain significant events in the Yukos saga unfolded: before Yukos' multiple settlement offers were ignored by the Respondent, before the Respondent seized and auctioned YNG, and before bankruptcy proceedings were commenced and Yukos was liquidated. These comments were made by Yukos' management and representatives with the reasonable belief (or at least legitimate hope) that the Russian Federation would act in good faith in its tax dispute with Yukos. As this turned out not to be the case, the Tribunal attributes little weight to this attempt by the Respondent to minimize the significance of the 15 April 2004 asset freeze.

(B) The failure to consider Yukos' proposals of alternative means of paying the tax assessments

98. The 15 April 2004 asset freeze effectively gave the Russian Federation the power to decide how Yukos' tax liabilities would be satisfied because it required Yukos to propose assets against which the bailiffs should enforce the levies. Under Russian law, the final decision on the assets against which enforcement would be made was reserved to the bailiffs.

99. The Claimants contend that the Tax Ministry's failure to respond to Yukos' numerous offers to settle or discharge its tax debt demonstrated that the Russian Federation had no interest in allowing Yukos to resolve its liabilities. It points to the following sequence of events (SoC ¶¶ 33, 141, 146):

30 June 2004	*Moscow Arbitrazh Court issues writ of execution. The Tax Ministry asks the First Interdistrict Office of the Court Bailiffs of the Central Administrative District of Moscow ("Bailiffs Service") to execute the judgment against Yukos and the Bailiffs issue an order giving Yukos five days to pay $3.5 billion.*
1 July 2004	*Yukos attempts to deliver to the Bailiffs a package of documents permitting execution against Yukos' 34.5 percent shareholding in Sibneft valued at $4.6 billion. The Bailiffs refuse to accept the package.*
2 July 2004	*Yukos writes to the Bailiffs Service requesting information on how to transfer the Sibneft stake. The Bailiffs do not respond.*
6 July 2004	*Former Canadian Prime Minister Jean Chretien writes to Prime Minister Fradkov on Yukos' behalf, proposing a payment of $8 billion as a global settlement for the 2000-03 tax years. No response is received.*

14 July 2004	*Bailiffs seize Yukos' shares in YNG. Yukos petitions the Moscow Arbitrazh Court to declare unlawful the Bailiffs' failure to execute against the Sibneft shares.*
15 July 2004	*Mr. Chretien writes again to Prime Minister Fradkov, reiterating Yukos' 6 July 2004 settlement offer.*
16 July 2004	*Steven Theede, Yukos' CEO, writes to the Minister of Finance requesting deferral of tax debt for six months or payment in instalments.*
30 July 2004	*Mr. Chretien writes to President Putin, reiterating Yukos' 6 July 2004 settlement offer.*
17 Aug. 2004	*Moscow Arbitrazh Court upholds the failure of the Bailiffs to execute against the Sibneft shares.*
30 Aug. 2004	*Deputy Minister of Finance writes to Yukos rejecting deferral request of 16 July 2004.*
16 Sept. 2004	*Yukos writes a letter to the Ministry of Justice proposing that the Bailiffs execute against Yukos' shareholdings in a number of companies, including Sibneft OJSC and Tomskenergo OJSC. The Russian Federation does not respond. Yukos reiterates its request on 24 November 2004, 25 November 2004, and 16 December 2004.*

The Russian Federation does not respond.

100. The Claimants emphasize that "Russia did not refuse or reject any of Yukos's 2004 proposals, it simply ignored them." (SoRep ¶ 298.)

101. The Respondent, however, contends that it had good reasons not to accept Yukos' purported settlement offers. First, Russian law does not require the bailiffs to execute against assets proffered by the debtor. Second, the Tax Ministry had no authority to grant Yukos' 16 July 2004 request to defer payment on the tax debt. Third, "[n]one of Yukos's offers were adequate or credible" because they would have required the Tax Ministry to: (i) accept the disputed Sibneft shares; (ii) accept a fraction of what was owed; or (iii) offset substantial VAT refunds that were not specified. (SoRej ¶ 240.)

102. The Tribunal is mindful that the Russian Tax Ministry, like tax authorities in other countries, had the discretion to decide whether to settle with Yukos. Indeed the ECHR has found that the Russian tax authorities "had a decisive freedom of choice" and "should have given very serious consideration to other options." (¶ 654.) The Tribunal is also sympathetic to the Respondent's contention that Yukos' settlement offers might not have been as appealing as Yukos had claimed; for example, questions linger regarding Yukos' title to the disputed Sibneft shares. Nevertheless, the Russian Federation's *failure even to respond* to the multiple offers by Yukos, the largest private taxpayer in Russia, in the view of the present Tribunal, raises significant doubts as to whether the Respondent acted in good faith in attempting to resolve its tax dispute with Yukos, and whether its actions were really taken as part of an ordinary process of assessing and collecting taxes. While ignoring multiple settlement offers by an ordinary taxpayer might seem odd, the failure of a tax authority to respond to multiple settlement offers by the State's largest private taxpayer is, in the Tribunal's view, highly suspicious; such treatment

of a major force of the national economy could not reasonably have been a matter of inadvertent clumsiness.

103. The Tribunal notes that "in February and March 2008, Rosneft was able to negotiate with the federal, regional, and local tax authorities an agreement that permitted it to pay off YNG's tax liability (assumed by Rosneft when it acquired YNG) over a five-year period starting in March 2008." (SoC ¶ 145.) In light of the fact that the Russian Tax Ministry had entertained and negotiated repayment plans with other large taxpayers, including Rosneft, the Tribunal accepts the Claimants' common sense argument that "[i]f the Russian Federation's true intent in the tax cases against Yukos was to collect legitimately-owed taxes, it would have worked with Yukos to find a way for the company to discharge its obligations that did not involve liquidation." (SoC ¶ 34.) The failure of the Russian Tax Ministry to work with Yukos, or to even respond to Yukos' multiple settlement offers, is disturbing to say the least.

(C) The seizure and sale of Yukos' shares in YNG

104. The Russian Federation seized and sold YNG to discharge Yukos' tax liabilities. The following events surrounded the YNG auction (SoC ¶ 36):

6 Oct. 2004	*Russia's appraiser, Dresdner Kleinwort Wasserstein ("DrKW") delivers a report to the Ministry of Justice valuing YNG at $15.7-$18.3 billion.*
7 Oct. 2004	*Press reports that the Ministry of Natural Resources is questioning the status of YNG's production licenses.*
18 Nov. 2004	*Bailiffs Service announces that YNG will be auctioned to satisfy Yukos' outstanding tax debt.*

19 Nov. 2004	*Russian Federal Property Service issues formal auction notice, setting a starting price of 246 billion roubles ($8.65 billion) for YNG.*
19 Dec. 2004	*YNG sold at auction for $9.3 billion to BaikalFinansGroup ("BFG".)*
22 Dec. 2004	*BFG purchased by Rosneft.*

105. As a preliminary matter, the Claimants contend that the seizure of YNG was disproportionate because, as noted by the ECHR, it "was capable of dealing a fatal blow to [Yukos'] ability to survive the tax claims and to continue its existence." (*Yukos v Russia*, ¶ 653.) The decision to auction YNG, so the Claimants say, "made sense only if the objective of the exercise was to place a crown jewel of the Russian oil industry under state control." (SoC ¶ 133.) According to the Claimants:

> *"If the Russian Federation's true intent was to collect taxes from Yukos, it had up to three years to do so. Waiting would have cost Russia nothing since interest would have continued to accrue on the Yukos liabilities. Nor would delay have entailed any additional collection risk, inasmuch as Yukos had the ability to pay in a reasonable time and the 15 April 2004 asset freeze gave Russia complete control over substantially all of Yukos's assets. There being neither a requirement nor a need for Russia to enforce its judgment against Yukos immediately, one is left to conclude . . . that the purpose of Russia's rapid use of the Moscow Arbitrazh Court's execution writ to seize YNG was motivated by a simple desire to put YNG into government hands, not by a wish to collect taxes." (SoRep ¶ 279.)*

106. The Claimants further allege that the YNG auction was conducted in a manner inconsistent with a *bona fide* exercise of the Russian Federation's taxation,

enforcement, and regulatory powers. They raise four series of complaints.

107. First, the Russian Federation did not attempt to maximize the price fetched by YNG at auction. To the contrary, the Federation tried to force down the auction price of YNG by imposing on it an additional $4.6 *billion* in new tax liabilities and raising questions about the validity of YNG's licenses. The additional tax liabilities were carried forward to Rosneft, but were ultimately reduced 84% by the Russian courts to $760 *million.*

108. Second, the Russian Federal Property Service did not use the standard procedure applicable to auctions of seized property, which would have required Russia to set YNG's starting price in line with DrKW's valuation of $15.7-$18.3 billion. Instead, the Russian authorities set the starting price of the YNG auction at $8.65 billion, significantly below the valuations in the DrKW report.

109. Third, the Russian Federation effectively barred privately-owned Russian oil companies and foreign oil companies from participating in the YNG auction by holding the auction only one month after announcing it, and by failing to encourage potential buyers to participate (*see generally* the Osterwald Report, who opined that a transaction such as this would normally have required a year or more in order to maximise revenue from the sale). The Tribunal notes that the Respondent chose not to cross-examine Mr Osterwald.

110. Fourth, the YNG auction was rigged: the sole bidder at the auction was BFG, "an unknown company with 'no telephone number, no office, [and] no corporate logo,' whose address is registered at 'a dilapidated building housing an off-license, a grocery, a mobile phone shop and the London Café, a favourite hangout of alcoholics and homeless people.'" (SoRep ¶ 349.) The auction lasted no more than 10 minutes, with BFG acquiring YNG with an uncontested bid for $9.3 billion. A few days after the auction and before payment of the purchase price was due, BFG was acquired by Rosneft.

111. The Respondent, however, disagrees with the Claimants' characterization of the YNG auction. As an initial matter, the Respondent emphasizes that the Russian courts have already reviewed and dismissed the Claimants' objections with respect to the YNG auction in upholding, *inter alia*: the Bailiffs' decision to enforce against Yukos' shares in YNG; the starting price of the YNG auction; that both BFG and Gazpomneft were *bona fide* participants in the YNG auction; and BFG's purchase of the YNG shares.

112. The YNG auction, according to the Respondent, was conducted professionally and in accordance with law. First, the Bailiffs complied with Yukos' request by choosing an auction procedure; the Bailiffs could have sold the YNG shares directly to a willing purchaser, at a potentially lower price. The Respondent therefore posits: "[I]f the Claimants' conspiracy theory had any substance, the Russian authorities would have simply sold the YNG shares directly to Rosneft, or any state-controlled company, in a negotiated deal not subject to any auction requirements. But the Bailiffs did not proceed by private transaction." (SoD ¶ 287.)

113. Second, Yukos is to blame for its own media campaign that "scare[d] potential bidders away from the auction of Yukos assets by threatening all bidders that were not frightened off that the winner would be plagued by a 'lifetime of litigation.'" (SoD ¶ 276.) The temporary restraining order ("TRO") issued by the Yukos-initiated U.S. bankruptcy court proceedings also deterred potential bidders. In other words, "Yukos, instead of maximising or trying to maximise the value of the YNG auction, [] actually minimis[ed] the value of the YNG auction." (T:Day 9:90:14-16.)

114. Third, the YNG auction was a public and legitimate auction (SoD ¶ 310):

> *"BFG did not bid against itself. It opened with a pre-emptive bid which, in a single move, placed its bid at half a billion dollars above the Starting Price. It is counterintuitive that an auction in*

which the participants were colluding would generate a bid US$500 million in excess of the Starting Price. If BFG was bidding against itself, it would have had no reason to raise the price at all, let alone significantly."

115. The present Tribunal endorses the findings of the *RosInvest* Tribunal regarding the YNG auction. (¶¶ 522-24.) On the one hand, the Tribunal is receptive to the Respondent's argument that some of the blame associated with the poor turnout and low winning bid at the YNG auction should be attributed to the Claimants for their media campaign threatening a "lifetime of litigation" and for initiating bankruptcy proceedings in the United States that led to the TRO. The Tribunal accepts the Respondent's argument that Yukos' actions reasonably could have deterred potential bidders from participating in the YNG auction.

116. On the other hand, the Tribunal finds many aspects of the YNG auction more than suspect. First, the Tribunal questions the Respondent's decision to seize and auction YNG. In light of the fact that the comprehensive asset freeze was in place and that interest would continue to accrue on Yukos' tax debt, the seizure of YNG seems to have been a drastic measure that, as the ECHR observed, "was capable of dealing a fatal blow to [Yukos'] ability to survive the tax claims and to continue its existence." (Yukos v Russia, ¶ 653.) The Respondent had less extreme alternatives at its disposal.

117. Second, the Respondent's decision to hold the YNG auction only one month after announcing it and the Respondent's apparent failure to solicit and encourange the participation of potential buyers in the auction seem to have affected the number of buyers and the corresponding number of bids. Mr Osterwald, a consultant with extensive experience with oil companies facing privatisation, market liberalisation, and restructuring, explained persuasively that the auction procedure was highly irregular in a number of ways that all relate to the extraordinary speed in which it was conducted. For assets

of this magnitude of value, Mr Osterwald observed, one would expect a number of professional advisers on valuation, a painstaking information memorandum, marketing materials and communication procedures with prospective buyers, a data room, more than one round of bidding to identify the more serious potential acquirers who would then be offered yet more comprehensive information, and throughout it all a sustained effort to generate interest on the international markets. Once a winner emerged, the ordinary practice would then be to engage in complex negotiations before ultimate closing. However, very little of this happened, which explains, doubtless, how the auction could have been carried out with such speed. Mr Osterwald opined that a transaction such as this would normally have required a year or more in order to maximise revenue from the sale. The Respondent has little to say in response, and chose not to put any question to Mr Osterwald. Tellingly, as it turned out only one company placed a bid at the YNG auction.

118. Paramount among the Tribunal's concerns relates to this sole bidder: BFG, an unknown entity, placed a $9.3 billion, uncontested winning bid for YNG, the largest oil production company in Russia, and was then acquired a mere three days later by state-owned Rosneft, even before payment of the purchase price was due. The Respondent has been unable to answer these key points, save to state that BFG is duly legally constituted as a corporate entity, and to rely upon subsequent endorsements by the Russian courts. The Respondent's argument, as summarized above, to the effect that YNG auction was of a public nature, and that BFG bid $500 million above the starting price, are insufficient to remove the suspicion of collusion, particularly when BFG was quickly taken over by Rosneft before payment of the purchase price was due.

119. Having carefully considered all the evidence and submissions on this issue, the Tribunal is unable to accept the legitimacy of this transaction, as pleaded by the Respondent.

120. Overall, the present Tribunal arrives at a conclusion consistent with the holding of the *RosInvest* Tribunal, namely that "there remain doubts whether the YNG auction can be seen as bona fide and non-discriminatory or as an expropriation for the public interest." (¶ 524.) Indeed, reviewing the sequence of events, the arbitrators in *RosInvest* were blunt, concluding in ¶ 620 that "the Tribunal is convinced that the auction of YNG was rigged." The Respondent has had more than a year since that conclusion was reached to adduce more persuasive evidence or argument before this Tribunal to rebut that finding. It has failed to do so.

121. Importantly for this Tribunal's enquiry, these findings lead once again to the conclusion that the conduct in question did not form part of an ordinary process of assessing and collecting taxes.

(D) Yukos' alleged imprudence, or bad faith, in not paying the tax assessments quickly and thus avoiding further pursuit

122. This is a *Leitmotif* in the Respondent's pleadings. If Yukos had quickly complied with the assessments instead of paying out vast sums in dividends for its shareholders, or securing its cash on hand behind the ramparts of off-shore legal entities, it would have been able to pay off its tax debt and ensure its survival – or so the Respondent argues.

123. The response to this argument can be very succinct. If Yukos' owners and management concluded that the Russian Government had set its face against them and was pursuing an objective of confiscation, they would hardly have been encouraged to keep profits sitting nicely where they could be taken by state power. If the storm clouds were so ominous, there was no reason to invest in assets within the jurisdiction (because they would be susceptible to dispossession by force) and the perfectly understandable reaction would be to save what could be saved of what is, after all, presumptively the property of any corporate entity's owners.

124. As for whether such apprehensions were justified, the present Tribunal, which has no mandate and no need to make a finding to that effect, nevertheless observes that the *RosInvest* Tribunal unambiguously found Russia's measures to have been "confiscatory." (¶ 574.) Whatever else might be said about the reactions of Yukos' management, there was nothing outlandish or exaggerated about its fear of abuse.

(E) Conclusion

125. The Tribunal recalls that the ECHR found that notwithstanding the "wide margin of appreciation," the Russian Federation prevented Yukos from discharging its tax debt and violated Article 1 of Protocol No. 1 by "fail[ing] to strike a fair balance between the aims sought and the measures employed in the enforcement proceedings." (¶¶ 651, 658.) The ECHR specifically took issue with "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." (¶ 657.) The ECHR refused, however, to find that Russia had misused the enforcement proceedings intentionally to destroy Yukos and take its assets. (¶¶ 665-66.)

126. On the other hand, the *RosInvest* Tribunal, not being bound by Protocol No. 1's "wide margin of appreciation," but rather by the terms of the applicable BIT, found that Russia's actions "must be seen as a treatment which can hardly be accepted as bona fide." (¶ 567.)

127. The present Tribunal has arrived at a conclusion consistent with the finding of the *RosInvest* Tribunal. As mentioned above, the timing and comprehensive scope of the asset freeze hindered Yukos' ability to pay its tax debt. Furthermore, the Russian Federation's failure even to respond to the multiple settlement offers by Yukos, the largest private taxpayer in Russia, raises significant doubts as to whether the Respondent acted in good faith in attempting to resolve its tax dispute with Yukos. More suspicious are the circumstances surrounding the seizure

and auction of YNG. The Respondent failed to take a number of actions that would have, according to the undisputed expert testimony of Mr Osterwald, increased the number of bidders and the corresponding bids. Tellingly, the YNG auction was won by the sole bidder, an unknown entity that placed a $9.3 billion, uncontested winning bid for YNG, the largest oil production company in Russia, and was then acquired a mere three days later by state-owned Rosneft before payment of the purchase price was due.

128. Accordingly, the Tribunal concludes that the 15 April 2004 asset freeze, the Russian authorities' failure to consider Yukos' proposals of alternative means of paying the tax assessments, and the seizure and sale of Yukos' shares in YNG demonstrate that the Respondent intentionally prevented Yukos from discharging its tax debt. As discussed above, this conclusion supports the Claimants' allegation that the Russian Federation's goal was to expropriate Yukos, and not legitimately to collect taxes.

7.3 Was Yukos' tax delinquency a pretext for seizing Yukos assets and transferring them to Rosneft?

129. Yukos was liquidated through involuntary bankruptcy proceedings, and its remaining assets sold in a series of auctions. The bankruptcy proceedings were closed on 15 November 2007, and Yukos removed from the Unified Register of Companies on 23 November 2007.

130. The Claimants allege that – as for each of the preceding steps – Yukos' tax delinquency was a pretext for this process, and for the ultimate seizing of Yukos assets and their transfer to entities controlled by the Russian Federation:

> *"[T]he Yukos bankruptcy proceedings were unnecessary and inappropriate if the goal of the Russian Federation was to collect taxes while at the same time protecting the collective interests of Yukos's creditors and shareholders. Under the circumstances that existed in 2006 – a single*

creditor of any significance, a freezing order that prevented dissipation of assets, and asset values that plainly would have allowed Yukos to pay all of its tax assessments without going through forced liquidation – the only plausible explanation for initiating bankruptcy proceedings and then liquidating, rather than reorganizing, Yukos was to facilitate and expedite the taking of Yukos's remaining assets and the transfer of them to new state-controlled owners. And the only plausible explanation for conducting the auctions as they were conducted – with no effort to create interest on the part of major foreign oil companies or to indicate even that they would be welcome as purchasers of the assets – was a desire on the part of the Russian Federation to ensure that the assets in fact were transferred to the designated state-controlled entities." (SoRep ¶ 373.)

131. Specifically, the Claimants take issue with the initiation of the bankruptcy proceedings, the rejection of Yukos management's restructuring proposal, and the conduct of the liquidation auctions:

"Using the Société Générale consortium as cover . . . the Russian Federation – acting through Rosneft – instigated a bankruptcy proceeding designed to transfer title to the remainder of Yukos's assets to selected state-controlled owners. With Rosneft and the Tax Ministry as Yukos's two largest creditors, the Russian Federation drove the bankruptcy proceeding, ensuring that Yukos management's proposal to restructure the company and pay off the remaining debts was rejected in favour of liquidation. The company's remaining assets were sold off in a series of questionable auctions. By the end of the process, Rosneft held 75 percent of what had formerly been Yukos, including all of its production properties." (SoC ¶ 164.)

132. The Respondent, however, maintains that the Russian bankruptcy and liquidation proceedings were

commenced and conducted in accordance with Russian law and procedure by Yukos' creditors.

133. As explained earlier, the question that arises for the present Tribunal is whether Yukos' tax delinquency was a pretext for the seizing of Yukos assets and the transfer of them to Rosneft or one of its affiliates. An affirmative answer would support the Claimants' theory that the Russian Federation's real goal was to expropriate Yukos, and not legitimately to collect taxes.

(A) Forcing Yukos into bankruptcy

134. The relevant sequence of events with respect to the bankruptcy proceedings was as follows. As a result of the asset freeze that took place on 15 April 2004, Yukos defaulted on a one billion-dollar loan issued by a consortium led by Société Générale. That consortium obtained an English court judgment for the outstanding amount of that loan, namely $472 million. On 8 September, the consortium applied for enforcement of that judgment by the Russian courts. But it did so in an unusual manner, entering into an agreement with Rosneft by which the latter would pay the $472 million in full in exchange for the consortium's promise to pursue bankruptcy proceedings against Yukos. As the Claimants ask rhetorically: Why not simply let the consortium get its judgment, assign it to Rosneft, and let Rosneft put Yukos into bankruptcy? The answer, according to the Claimants, is that this could only have been for the sake of appearances, instead of a sequence in which an entity owned by the very State which had prevented Yukos from making the payment in the first place then proceeded to the liquidation of the company:

> *"[B]y March 2006, both the Tax Ministry and Rosneft itself (by virtue of claims asserted against Yukos by YNG, now part of Rosneft) could have taken steps to initiate bankruptcy proceedings against Yukos. Instead, the Russian Federation engaged in an elaborate subterfuge to create the*

impression that it was private creditors, not the Russian state, that were responsible for initiating the bankruptcy of Yukos." (SoC ¶ 168.) *"...the only explanation for that requirement [that the Société Générale consortium initiate bankruptcy proceedings against Yukos] is that the Russian Federation wished to obscure who was behind the initiation of the bankruptcy."* (SoRep ¶ 359.)

135. Once the Moscow Arbitrazh Court had accepted the consortium's bankruptcy petition, Rosneft assumed Yukos' debt from the consortium and, with the court's approval, stepped into the shoes of the consortium in the bankruptcy proceedings. Rosneft's purchase of the consortium loan left it and the Russian Federation as the only creditors of any significance. As the Claimants observe, and as the Tribunal agrees, this sequence of events was at odds with the underlying purpose of the bankruptcy law – it was "more consistent with the use of insolvency as a device for gaining control of assets rather than satisfying debt." (Westbrook Report, ¶¶ 11-12, 23.) In the Claimants' words:

> *"With the Tax Ministry and Rosneft together holding virtually all of Yukos's external debt, a bankruptcy proceeding was not needed to protect any collective interest. Nor did the Russian Federation need a bankruptcy in order to secure Yukos's assets: the asset freeze of 15 April 2004 and subsequent orders already prevented Yukos from disposing of its assets without the authorities' permission . . . The only plausible purpose served, then, by bankruptcy proceedings dominated by the Tax Ministry and Rosneft was to facilitate the taking of Yukos's remaining assets and their transfer to new state-controlled owners by replacing an uncooperative Yukos management with an administrator effectively appointed by the Tax Ministry and Rosneft."* (SoC ¶ 173.)

136. The Respondent, on the other hand, defends the initiation of the bankruptcy proceedings, asserting that:

"there was no subterfuge or impropriety in connection with the Russian bankruptcy proceeding, which was conducted in full conformity with Russian bankruptcy law." (SoD ¶ 332.)

137. First, neither the Claimants nor Professor Westbrook "cite[d] a single legal provision or procedural requirement of Russian law that might have been violated." (SoD ¶ 343.)

138. Second, Yukos' bankruptcy was inevitable because Yukos was unable to meet its debts as they came due. Indeed, Yukos' management had filed a voluntary petition for bankruptcy in the United States on 14 December 2004.

139. Third, Rosneft's obligation to purchase the consortium's debt was not dependent on the Société Générale consortium initiating bankruptcy proceedings against Yukos. The purchase price was payable on the earlier of either 28 April 2006 or the second business day following the initiation of bankruptcy proceedings against Yukos. (As it later turned out, the bankruptcy proceedings were initiated on 9 March 2006.) Furthermore, the decision of the Société Générale consortium to trigger Yukos' bankruptcy was reasonable:

> *"The logic of the Assignment Agreement is clear. Yukos was in default on a half billion dollar obligation to western banks. The SocGen Consortium had proceeded to obtain a court judgment recognizing that obligation. That court judgment was a necessary predicate to instigating Yukos's bankruptcy. Thus, because the SocGen Consortium (but not Rosneft) had a judgment in hand, Rosneft apparently agreed to acquire the credit more quickly if the SocGen Consortium placed Yukos in bankruptcy (thereby avoiding any need for Rosneft to seek a court judgment itself in order to be in a position to initiate a bankruptcy against Yukos.)"* (SoD ¶ 351.)

140. Fourth, the Rosneft-Société Générale consortium agreement was not confidential: it was "an open, arms-length deal" that was disclosed by Rosneft in its US GAAP financials. (SoD ¶ 352.) Although the agreement contained a confidentiality clause, such clauses are normal in commercial agreements and this one was temporary in nature.

141. The Tribunal has carefully considered each of the Respondent's defences, but is ultimately unpersuaded by them. The issue here is not one of the legality of the bankruptcy proceedings, nor their conformity with Russian bankruptcy regulations. Rather, it is whether the steps that were taken can properly and fairly be characterised as part of an ordinary process of collecting taxes. In the Tribunal's view, they cannot fairly be so characterised, particularly when viewed against the broader chronology of which they form part (as summarised later in this section). This conclusion is not overcome by the Respondent's various technical analyses of the consortium agreement.

(B) The rejection of the management restructuring plan

142. The Tax Ministry and Rosneft were Yukos' largest creditors, between them controlling 94 percent of the votes at the first meeting of creditors, which took place on 20 and 25 July 2006.

143. Even at this late stage, Yukos proposed a restructuring pursuant to which it would immediately sell off $15.7 billion worth of core assets, and use $1.5 billion held in the Netherlands to pay off other creditors – including Rosneft as the Société Générale consortium's assignee. This would have left Yukos with core assets valued at $20.5 billion, which the Yukos management team explained could generate some $3 billion per year to pay off the remaining recognised claims.

144. The Claimants maintain that Russia used its control of the meeting of creditors to ensure that this restructuring proposal put forward by Yukos' management was rejected, and instead that the decision was taken to liquidate the company's remaining assets:

> *"The restructuring proposal was considered at the meeting of creditors held on 20 and 25 July. Out of a total of 23 creditors represented at the meeting, 6 cast ballots in favour of accepting the restructuring proposal and three abstained. The proposal was nonetheless rejected by an overwhelming majority of the debt-weighted votes because it was opposed by the Tax Ministry, Rosneft and YNG, together with one minor creditor. This decision was upheld by the Moscow Arbitrazh Court on 5 August 2006, and opened the way for the distress sale at auction of Yukos's remaining assets between June 2006 and November 2007."* (SoC ¶ 177.)

145. The Claimants contend that the Respondent's proffered reasons for the creditors' rejection of the restructuring proposal are simply "post hoc rationalization[s]." (SoRep ¶¶ 364-65, 367, 370.)

146. The Respondent, however, maintains that the decision to liquidate fully complied with Russian law. Furthermore, there were reasonable grounds for Yukos' creditors to prefer immediate liquidation and recovery of their claims to a plan that left their fate in the hands of Yukos' management. In particular, the management restructuring plan: (i) proposed to pay Yukos' debts over two years, but there was no assurance that Yukos would succeed; (ii) proposed to allow Yukos to retain its core assets, leaving the creditors to satisfy themselves with low-value and high-risk assets; and (iii) lacked appropriate evidence to support Yukos' valuation of its assets. (SoD ¶¶ 363-64.) The creditors also feared that "Yukos's management would continue their dissipation of assets if left in charge of Yukos." (SoRej ¶ 292.) In short, there was nothing unusual about the creditors'

decision to reject Yukos' rehabilitation plan, as illustrated by Russian practice:

> *"In Russia, only a de minimis number of Russian bankruptcy filings ever enter financial rehabilitation procedures. For instance, in 2002, of the 94,531 insolvency claims successfully filed in the Russian Federation, none entered financial rehabilitation. In 2003, only 10 of the 9,695 insolvency cases filed entered rehabilitation. In 2004, the statistic is just 29 out of 10,093. And in 2005, the year before the Yukos creditors' meeting, only 32 out of 25,643 insolvency cases entered financial rehabilitation. Of all the cases that entered rehabilitation between 2002 and 2005, only three resulted in the debtor actually discharging its debt. Rehabilitation plans are only accepted in the most extraordinary circumstances—and certainly not when the company's plan is based on speculative, unrealistic figures, presented by a management that had repeatedly acted in an openly hostile manner towards its creditors."* (SoRej ¶ 285.)

147. Once again, the issue is not whether the rejection of the management restructuring plan, and the decision to liquidate, fully complied with Russian law or practice as a technical matter. Rather, the issue is how these events are fairly to be characterised. Judged in abstract, the Respondent's submissions to justify the preferences of the Yukos creditors (i.e. immediate liquidation and recovery of their claims) are understandable. But the Tribunal's enquiry cannot be compartmentalized in this way and, as set out later in this section, once set against the wider context, the choices and actions of Yukos' main creditors clearly appear part of an overall confiscatory scheme.

(C) The liquidation auctions

148. The Claimants maintain that the Russian Federation manipulated the liquidation auctions to ensure

that it paid an effective price of zero for Yukos' remaining assets. The starting prices at the liquidation auctions, say the Claimants, were set lower than the independent valuations that the court-appointed manager was required by law to obtain. Furthermore, there was an absence of genuinely competitive bidders at the liquidation auctions:

> *"In an insolvency auction properly advertised and conducted, with neither collusion nor intimidation to affect the bidding, one would expect the presence of a number of qualified bidders from among the major oil companies as well as from some of the numerous large independent companies in the industry. One would anticipate vigorous bidding. In the Yukos case, however, very few bidders appeared at the auctions; those who did appear were largely unknown to the industry's expert observers; and the bidding was short and generally finished near the opening price. The end result of the auctions was that the greater part of the value of these assets was acquired, directly or indirectly, by the Russian state petroleum instrumentalities. This outcome is not what one would expect in a properly conducted insolvency auction."* (Westbrook Report, ¶ 18.)

149. At the merits hearing, Ms. Cheek further elaborated on the significance of the absence of competitive bidders:

> *"Many of the auctions . . . weren't highly contested. The ones for Transneft and Samaraneftegaz, the two most valuable assets coming out of the bankruptcy, the only bidders were Rosneft and previously unknown entities that appeared to be set up just so that there was a second bidder at the auction. So by dollar value . . . Rosneft ends up owning 75 per cent of Yukos's assets that were seized in auction by the state.*
>
> *But that doesn't tell the complete picture . . . [A]n unknown company named Prana wins the auction for Yukos's headquarters but Rosneft basically*

purchases these assets shortly after the auctions take place, increasing Rosneft's ownership to 84 per cent of Yukos's former assets . . .

[Yukos' Sibneft] shares were auctioned off as part of the bankruptcy process and while they were purchased by Italian company ENI, ENI had executed an agreement with Gazprom, Russia's state gas company, whereby Gazprom could exercise its option to buy that 20 per cent stake in Sibneft. It ultimately exercised that option. Therefore, those assets as well end up in the hands of the Russian state.

So when you add up these various pieces at the end of the day . . . the Russian Federation has ended up with 93 percent of Yukos Oil Company." (T:Day 1:192:5-25, 193:1-10.)

150. The Claimants also contend that Yukos' shareholders received no benefit from the sale of the company's assets because the Russian Federation manufactured liabilities sufficient to absorb all of the revenue generated by the liquidation auctions. The Claimants posit that "Russia ensured that it paid a net price of zero for Yukos: whatever Rosneft and Gazprom paid for Yukos assets in the auctions found its way back into the Russian Federation's pockets as repayment for fictional liabilities." (SoC ¶ 185.)

151. The Respondent, however, insists that the liquidation auctions complied with both Russian law and international practice.

152. First, the starting prices used at the liquidation auctions were, in accordance with Russian law, based on the market value of the auctioned property as determined by the Roseko Consortium. Tellingly, the Roseko Consortium's conclusions and methodologies were never challenged by Yukos' creditors or shareholders.

153. Second, the price achieved at each liquidation auction was higher than the starting price. Moreover, the

auctions cumulatively produced approximately $2.3 billion more in proceeds than the estimate in the Yukos management rehabilitation plan.

154. Third, there was in fact genuine competition at the liquidation auctions. Russian law requires a minimum of two participants, and this requirement was met for all of the liquidation auctions. Furthermore, the court-appointed bankruptcy manager took the following actions to promote auction attendance: (i) he publicly announced the auctions thirty days in advance; and (ii) he placed no restrictions on participation in the auctions. By contrast, the Claimants are to blame for their "threats to impose a lifetime of litigation on the successful bidders" that contributed to the poor turnout and correspondingly low bids. (SoD ¶ 375.)

155. Finally, the significance of the fact that Rosneft or Rosneft affiliates won the majority of the liquidation auctions is unclear:

> *"To win approximately one-half of the auctions, Rosneft borrowed US$22 billion from world leading financial institutions and paid for the assets acquired. The fact that Rosneft succeeded in approximately one-half of the auctions simply means it valued the assets more highly than others. It also means Rosneft did not participate or prevail in the other half. The remaining eight (out of seventeen) auctions were won by private bidders – including Enineftegaz, Monte Valle, JVP Investments, Novatek, Prana, TsentrInvest-Tradig, and Promneftstroy – who collectively paid a total of RUR 276,265,364,044 for the assets they acquired."* (SoD ¶ 378.)

156. The Tribunal is unpersuaded, as a technical matter, that the liquidation auctions were conducted in breach of Russian law or practice, and accepts the various and detailed submissions of the Respondent in this regard.

157. But the Tribunal also notes that, as a result of these auctions, "at the end of the day . . . the Russian

Federation has ended up with 93 percent of Yukos Oil Company." (T:Day 1:193:1-10.)

158. As summarised below, the overall chronology of which the liquidation auctions form part, casts them and their outcome in a particular light. After careful consideration of the entire record, the Tribunal concludes that, as with the preceding events, the liquidation auctions were part of the same overall scheme of confiscation. In this regard, the Tribunal's findings are consistent with those of the *RosInvest* Tribunal (¶¶ 567, 574.) The ECHR's finding to the contrary – *i.e.*, that Yukos failed to prove that the Russian Federation "had misused those [enforcement] proceedings with a view to destroying the company and taking control of its assets" – must be understood as based on a heightened requirement of "incontrovertible and direct proof," given the "wide margin of appreciation" a State enjoys under Protocol No. 1 to the European Convention on Human Rights. (¶¶ 659, 663, 665-66.)

(D) Conclusion

159. The present Tribunal endorses the conclusion of the *RosInvest* tribunal, which was unable to "find any evidence on file sufficiently showing that these [liquidation] auctions were either breaching Russian law or even breaching the higher standards to be applied under the IPPA." (¶ 535.) This Tribunal agrees. The Claimants in this proceeding have failed to demonstrate that the manner in which the bankruptcy and liquidation proceedings were commenced or conducted violated Russian law.

160. But as already noted several times, that is not the present issue. The Tribunal in this case is concerned with whether Yukos' tax delinquency was actually a pretext for the seizing of Yukos' assets and the transfer of them to Rosneft or one of its affiliates. And on this point, the Tribunal must take into account all the circumstances of this case.

161. Some of the key features of this part of the chronology which have been emphasised by the Claimants, and which have persuaded the Tribunal in its characterisation of the Respondent's conduct, may be distilled, briefly, as follows.

162. Yukos managed (under protest) to pay nearly two-thirds of the initial $3.5 billion levy by the end of August 2004. Given the disparity between the residual amount due and the value of YNG, which accounted for 60% of Yukos' production and had been seized in mid-July, the Tax Ministry set about raising new tax claims. These were assessed in tranches of multiple billions of dollars, e.g., on 16 November, when Yukos was ordered to pay $6.8 billion the next day. Meanwhile, Yukos' staff lawyers and independent counsel were arrested and charged with embezzlement.

163. YNG was ultimately sold at auction for $9.3 billion, not much more than half of the value appraised by the Respondent's own advisers, Dresdner Kleinwort Wasserstein, to an unknown company (BFG).

164. But even with the loss of YNG, Yukos' remaining assets were capable of producing more than half a million barrels of oil per day – a value of macroeconomic dimensions. Bankruptcy is conventionally understood as the resolution of conflicting claims by creditors. Yet Yukos had only one creditor that counted: the Russian Federation, with 94% of the vote in the debtor's collegium. The bankruptcy resulted in the eviction of Yukos' management and its replacement by a bankruptcy administrator, Mr Rebgun.

165. Not only did the Respondent then reject the management restructuring plan, but Mr Rebgun, the administrator, chose not to file the paperwork which would have entitled Yukos, under the very requalification of intergroup transfers which had led to such massive tax assessments, to recover in excess of $10 billion in VAT refunds from exports now attributed to it.

166. Nor did Mr Rebgun seek to test yet another tax assessment, this one on account of FY2004 in the amount of $3.7 billion. He simply added it as an additional debt to the Tax Ministry.

167. By mid 2006, of course, the international oil markets were forcefully ascendant and Yukos' book value was vastly understated. Yet Yukos' remaining assets were auctioned off in August, with Rosneft successfully bidding in 9 of the 17 auctions; these were the important ones, representing 75% of the value, including the two remaining large Yukos-producing assets, Transneft and Samaraneftegaz. One of the other successful bidders was an unknown company by the name of Prana, which acquired Yukos' headquarters buildings – but promptly resold them to Rosneft with the result that Rosneft in fact ended up with 84% of the assets in bankruptcy.

168. On 23 November, Yukos was removed from the register of companies; its shares were legally extinguished.

169. In due course, another State-owned entity, Gazprom, acquired a final major Yukos asset, namely its 20% share in Sibneft, which had been purchased by a third party and in turn had granted an option to Gazprom to resell them. That option was exercised. In the end, the result of Yukos' bankruptcy was to put 93% of its assets into the hands of State-owned entities.

170. This sequence of events took place in circumstances where (1) the Tax Ministry had no competing creditors with whose interests a reconciliation was necessary, and (2) the interests of the Russian Federation were at any rate protected by the asset freeze. Had Yukos been given a moment to catch its breath and to encumber or disperse of its assets in an orderly fashion, it appears that it could have paid its tax bills, since its fundamental asset portfolio was sound. That is how a legitimately operating tax authority would have proceeded.

171. Further, under the law (Article 321 of the Arbitrazh Procedure Code) the tax authorities had three years to enforce its assessments. That would have given Yukos a respite until some time in 2007. Instead, its prime asset – YNG – was seized and sold at an auction by December 2004. As the ECHR put it, at ¶¶ 656-7 of its judgment in *Yukos v. Russia:*

> *"... 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 .... the Court finds that the domestic authorities failed to strike a fair balance between the legitimate aims sought and the measures employed."*

The ECHR did not reach this conclusion without having given some weight to Russia's arguments to the effect that the tax authorities were operating under procedural constraints. The present Tribunal is not persuaded, having had the benefit of extensive debates and documentation, that there was a need to recognise such constraints. On any view, the enforcement of the tax assessments was a complex operation involving massive financial stakes, which any tax collection agency anywhere, if operating rationally and respectfully of the taxpayer's rights, would have conducted with the greatest care to maximise both recovery and preservation of enterprise value. The Respondent's suggestion that it was necessary to operate with utmost speed by reason of its own regulations is powerfully counter-intuitive, and in fact not born out by the evidence.

172. The timing of key events bears repeating. The *ex parte* freeze on all of Yukos' assets took place on 15 April 2004, the very day after the Tax Ministry's demand for $3.5 billion in taxes on account of FY2000. The *next day* was imposed as the deadline for voluntary payment. A writ of execution was issued on 30 June, and on 14 July Yukos' shares in three subsidiaries, first and foremost YNG, but also Samaraneftegaz and Tomskneft, were

seized by execution officials. Within days (in fact on 20 July) the Ministry of Justice announced its intention to sell YNG to satisfy the tax judgment.

173. This announcement was obviously something of a bombshell in the industry, in terms of suggesting to the market that Yukos was collapsing. It was so precipitate, in the Tribunal's view, as to exclude any innocent explanation. This treatment of a major force of the national economy could not reasonably have been a matter of inadvertent clumsiness.

174. The three-year limit, the Respondent argues, should not be understood as a brake on enforcement proceedings. The question it put to its Russian law expert, Mr Rozenberg, was whether under Article 321 the Tax Ministry "could and should have waited up to three years before commencing the execution procedure against Yukos." But this is not the issue at all. The Tribunal takes for granted that tax authorities in a good system of governance could seek to collect monies due to the Treasury with expeditiousness – but also with rational care and respect for the rights of the taxpayer.

175. Such a rational arrangement was in fact worked out with Rosneft, whose own tax liabilities were, as appears from its consolidated financial statements, consensually scheduled for repayment quarterly over five years. Yukos contends today that it had cash flows sufficient to pay the assessed taxes. (In hindsight, this assertion is made all the more plausible having regard to the evolution of oil prices since then.) Whatever the arguments might have been as to Yukos' solvency, the fact is that it was a gigantic enterprise whose valuation would have required extensive study. The Respondent may have marshalled arguments since then as to why Yukos was not as solid as is contended by its old owners, but what is missing – and thus supports the plain inference that the Respondent's objective was the subjugation of Yukos, not the orderly collection of normal taxes – is its inability to show such an investigation *preceding* its decision, in effect, to dismantle Yukos. Indeed, as the

Claimants stress, Yukos had almost entirely paid off the 2000 tax assessment, i.e. the raison d'être of the seizure in the first place, by the time YNG was auctioned off. The valuation commissioned by the Respondent itself suggested that YNG was worth many multiples of the Yukos assessment on account of TY2000.

176. The Respondent argues today that Yukos could have solved the problem by causing its subsidiaries to sell off their assets and pay the proceeds as dividend to Yukos. It is however implausible to contemplate that the Russian authorities would have allowed the value of the very assets that were frozen to be diluted in this fashion.

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

7.4 The relevant enquiry

178. The debate in this case is not about whether the Respondent engaged in an *illegal* expropriation, but whether its measures were in fact expropriatory, within the scope of Article 6 of the BIT. If so, the BIT recognises the duty of compensation, and sanctions its failure through the decisions of tribunals such as the present one.

179. The notion that states have a considerable margin of discretion in enacting and enforcing tax laws should not lead to any confused idea that they have a discretion as to whether or not to comply with an international treaty. True enough, as *RosInvest* put it, "States have a wide latitude in imposing and enforcing taxation laws even if resulting in substantial deprivation without compensation" (¶ 580). Yet there is a world of difference between incidental detriment, even of a substantial nature, and purposeful dispossession. It is no answer for a state to say that its courts have used the world "taxation" – any more

than the word "bankruptcy" – in describing judgments by which they effect the dispossession of foreign investors. If that were enough, investment protection through international law would likely become an illusion, as states would quickly learn to avoid responsibility by dressing up all adverse measures, perhaps expropriation first of all, as taxation. When agreeing to the jurisdiction of international tribunals, states perforce accept that those jurisdictions will exercise their judgment, and not be stumped by the use of labels.

180. Moreover, in contradistinction to *Yukos v. Russia*, which arose in a forum which recognises the minimum human rights that exist irrespective of specific promises to the plaintiff, and indeed allows actions by a national against his own State, in this case it behoved the Respondent to consider that its treatment of Yukos would affect the rights of Spanish nationals, protected by specific treaty obligations.

181. The preceding observations are not meant to suggest that international tribunals should quickly reach the conclusion that ostensible tax measures are in fact compensable takings. To the contrary, the presumption must be that measures are bona fide, unless there is convincing evidence that, upon a true characterisation, they constitute a taking. Given the infinite variety of forms which can be given to a process having the result of expropriation, the effectiveness of the rule of international law in this regard necessarily requires, in each case, a comprehensive assessment of the factual circumstances that have led to the loss of which a claimant complains.

182. As Professor Christie wrote in his familiar article in 1962 ("What Constitutes a Taking of Property under International Law?" 1962 *BYIL* 307):

> *"it is evident that the question of what kind of interference short of outright expropriation constitutes a 'taking' under international law presents a situation where the common law method of case by case development is pre-eminently the*

best method, in fact probably the only method, of legal development."

183. In recent years, the texts of investment treaties illustrate the concrete implications of this. For example, the identical Annexes on Expropriation to the RTAs concluded between the US and Australia, Chile, Central America, Morocco, and Singapore, as well as to the 2004 US Model BIT, which provide that:

> *"the determination of whether an action or series of actions by a Party, in a specific fact situation, constitutes an indirect expropriation, requires a case-by-case, fact-based inquiry ....."*

184. The Tribunal has noted the distinguished *RosInvest* arbitrators' overall conclusion to the effect that:

> *"the totality of Respondent's measures were structured in such a way as to remove Yukos's assets from the control of the company and the individuals associated with Yukos. They must be seen as elements in the cumulative treatment of Yukos for what seems to have been the intended purpose* (¶ 112) *... [Yukos] was subjected to relentless and inflexible attacks ... [that] can only be understood as stages under a common denominator in a pattern to destroy Yukos and gain control over its assets"* (¶ 621).

185. This key passage led the arbitrators to conclude that the Respondent's measures, "seen in their cumulative effect towards Yukos, were an unlawful expropriation" under the relevant treaty.

186. In this case, the Tribunal's mandate is not to decide whether there has been an unlawful expropriation, but whether there has been an expropriation at all. This conclusion does not require findings of subjective intent or animus, as suggested by the words "purpose" and "relentless". Clearly the *RosInvest* holding comports a

finding of expropriation – *qui peut le plus peut le moins* – and the conclusion of the present award, which is constrained to answer only the lesser question, is therefore consistent both with *RosInvest's* conclusion and the aggregating approach of its analysis of the relevant events.

7.5 Adequate compensation

(A) The Claimants' approach

187. The Claimants argue that they should be compensated in an amount equal to their proportionate share of Yukos' market value on 23 November 2007 as it would have been but for the Respondent's expropriatory measures. The Claimants together held 73,000 shares (or more precisely their equivalent in ADRs); Yukos as a whole had some 2.2 billion outstanding shares. Yukos' overall value, they say, would have been $83 billion, leading to proportionate compensation to them in the amount of $2,625,810, plus interest.

188. This compensation purports to be consonant with the customary international law standard for recovery in the event of lawful expropriation and Article 6 of the BIT. (The Claimants conceded in the jurisdictional phase of this arbitration that they could not, under the terms of the BIT, seek compensation for unlawful expropriation. *See* Section 6.1.)

189. The date of 23 November 2007 corresponds to the "time of the taking" or, in this case, the date when Yukos was removed from the Unified Register of Companies in the wake of the end of the bankruptcy proceedings as pronounced by the Moscow Arbitrazh Court.

190. The Respondent questions the date of 23 November 2007, asking "how Claimants can argue that the alleged expropriation occurred in November 2007, which was several years after most of the alleged expropriatory events of which they now complain, and over a year after they gave notice of their expropriation claim." (SoRej ¶ 443.) The Respondent further asserts that as it denies that "any expropriation occurred at all, it

is certainly not incumbent on the Respondent to put forward alternative dates on which such a non event may have occurred." (SoD ¶ 477, n. 822.) If the Respondent could propose more appropriate dates, it might prudently have advanced such contentions in the alternative, rather than simply denying that its measures had the effect of an expropriation. Having rejected that denial, the Tribunal accepts the Claimants' logic in putting forward the date as 23 November 2007.

191. The notion of "expected" value refers to the fact that the market value on 23 November 2007 was nil, and therefore must be compensated by reference to what one may conclude the valuation of Yukos as a going concern would likely have been if the business had been unimpeded by the Respondent's expropriatory conduct. Compensation "should exclude any decline in value attributable to the threat of a taking", so the Claimants argue, and therefore "the appropriate methodology is for the Tribunal to base its valuation on the last price before the threat of a taking rendered the stock price an unreliable indication of Yukos' worth." (SoC ¶ 217).

192. The Claimants put forward 14 April 2004 as the date of the "last reliable stock price" for Yukos, $14 per share, because this was immediately before the news of the Tax Ministry's tax claim for Y2000 and the asset freeze of 15 April, resulting in a significant departure in the trend of Yukos' stock price.

193. The Claimants rely on the expert evidence of Professor Richard S. Ruback of the Harvard Business School, who proposed a value of $35.97 on 23 November 2007 by considering the relationship between the evolution of Yukos' share price as compared to a cohort of four of its Russian oil and gas competitors prior to 14 April 2004, and then projecting that relationship from 14 April 2004 to 23 November 2007 in order to estimate Yukos' share value in the absence of the Respondent's measures.

194. Professor Ruback also "confirmed" his estimate by looking to the value of Rosneft, which went public in July

2006 and which acquired most of Yukos' assets. His use of three different metrics suggests to him that the market value of "legacy-Yukos assets owned by Rosneft" was somewhere between $72-$91 billion at the valuation date, to which should be added the proceeds from the liquidation auctions of other Yukos assets, leading to a valuation of Yukos in the range of $83-$102 billion.

(B) Comparison with *RosInvest*

195. The Tribunal finds it somewhat difficult to follow *RosInvest's* reasoning with respect to the discount applied to the valuation of the investors' shareholding inasmuch as it focused on their having made a "speculative investment." (¶ 668 et seq.) The word "speculative" has no defined meaning that allows one to identify "non-speculative" investments. All investments are in some sense ultimately speculative. Investors' appetites depend on how much they are putting at risk, how much may be gained, and the chances of success. Even though the odds are identical, more people are willing to "invest" $1 for a remote chance at winning $10,000 than are willing to "invest" $10,000 for an equally minute chance at winning $100 million.

196. On the other hand, putting aside the word *speculative* and focusing on the analysis in *RosInvest*, one returns to familiar territory. As that tribunal indicated in ¶ 666, the arbitrators accepted "Claimant's assertion that it made an investment at such a point in time when the market had in fact overreacted to transient events and the price of the shares was unjustifiably low" but rejected its overly "optimistic expectations regarding the future development of the value of the investment." This is a straightforward reflection of the commonplace phenomenon that claimants tend to place a high value on the property of which they have been deprived.

197. In *RosInvest*, the final claim was for US$232.7 million (excluding interest), being the alleged loss of shareholding value as of 15 August 2007, which the Claimants identified as the date on which the Respondents' expropriation of Yukos' assets was

complete. That case involved a number of features which are different from those of this arbitration, such as the manner of RosInvest's acquisitions of its Yukos shares, and possible others which are not apparent without full access to the record in that case. Still, it is evident that the claim essentially posited a pro-rata share of the hypothetical value of Yukos but for the Respondent's measures. RosInvest argued, as the Award puts it in ¶ 645, that to allow the Respondent to "retain more than 96% of Claimant's share of the value of Yukos assets . . . would simply reward Respondent for its unlawful actions". Still, after noting that the dates of RosInvest's two purchases of Yukos shares – in the total amount of 7,000,000 shares – were 16 November and 1 December 2004, when "the market had 'priced in' the likelihood and effect of the Russian Federation's actions in respect of Yukos" (¶ 665), the Tribunal limited its award to the principal amount of $3.5m, which is what the arbitrators found to be its undisputed purchase price for the shares (paid only on 24 January 2007, for reasons not relevant here). (¶ 675.)

198. If one applies his approach in the present case to *RosInvest*, Professor Ruback would apparently have valued RosInvest's shareholdings at $251,790,000 (albeit as of 23 November 2007, rather than 15 August 2007 as the *RosInvest* arbitrators did). In other words, the actual *RosInvest* award was only 1.39% of what Professor Ruback suggested was correct. Contrariwise, it might be said that the *RosInvest* Tribunal's approach to valuation, if applied to the present case, would have led to the very modest recovery of $663,050 – simply taking the present Claimants' purchase price for their shares as "the best reflection of the damages." (¶ 675.)

199. The reason why it would be improper to apply Professor Ruback's approach to the *RosInvest* situation (an approach which Professor Ruback himself has of course not endorsed) may be expressed in a single word: timing. At the time of RosInvest's purchases, Yukos was all but doomed and retained only the residual value of hope for recovery through a process of legal claims. At

the time of the present Claimants' purchases, on the other hand, significant events leading to Yukos' demise had not yet occurred. For example, the Claimants purchased all of their Yukos stock before Russia seized Yukos' shares in YNG; before Russia announced that it would sell YNG; before Yukos exhausted its appeals against the $3.5 billion tax claim for 2000; and before the tax authorities imposed billions of dollars in additional tax liabilities against Yukos for the 2001 to 2003 tax years. (SoRep ¶464.) It is a familiar tenet of international law that compensation cannot be reduced on the basis that anticipation of expropriating conduct has depressed the market value of the asset.

200. RosInvest bought its Yukos' shares for an average price of less than US$1 per share in November and December 2004. The last of the present Claimants' purchases was on 7 July that year. Those months made a large difference.

201. By way of perspective, in early 2002, Yukos' shares had traded at around $10. The first of the various Claimants' purchases was made on 19 December 2003 and the price was still at $10.80. Despite clouds on the horizon, Quasar de Valores' purchases on 20 February 2004 were at $12.45, and the price climbed further, to around $15, in the following two weeks. Although the tax claims against Yukos depressed the price to around $6 by early June, an announcement by President Putin on 17 June that there was no intent to bankrupt Yukos resulted in a 35% share increase on 17 June. Two other Claimants bought shares on 7 July, but the announcement by the Ministry of Justice on 20 July that Yuganskneftegaz would be auctioned led to a 17% drop. Still, the bottom did not fall out until December, when the auction was actually carried out. Since then the share price has been an almost flat line, sloping slowly in the downward direction from $1 until 23 November 2007. The last price at which it was possible to purchase Yukos shares was $0.23.

202. In sum, the RosInvest purchase in December 2003 was very much of a different nature than those of the Claimants here. The former involved a bet that something might be salvaged, somehow, from the Yukos carcass – perhaps buying at $.50 to sell at $1 – with no prospect of resuscitating Yukos as a going concern, but might still be generate 100% profit. The Spanish purchases, on the other hand, assumed that Yukos would not be treated unlawfully by the State, and that Yukos' assets and potential as an enterprise could overcome the losses caused by its exceptional tax debts as of that date. This assumption they were entitled to make, and to rely upon as a matter of international law by virtue of the BIT.

203. Put another way, the Claimants' purchases came at a time when the Respondent's series of actions against Yukos was still far from having run its course. The Claimants cannot be faulted for having relied on the proposition that the Respondent would in the end adopt a different course than the *de facto* expropriation of Yukos. What they bought (Yukos shares in the December 2004-July 2004 period) was assuredly not a stake in an untroubled concern managed in unimpeded fashion by a cohort of stellar managers, successfully exploiting a dazzling array of hydrocarbon assets. Yukos' managers were under indictment and its debts were mounting. The market reflected that bitter change in fortunes. But what was left was still of considerable potential value, assuming the corporate body was allowed to mobilise its remaining resources without unlawful interference. The value of that residual potential is what the Claimants were free to seek to capture; and when that legitimate expectation was defeated by the ultimate completion of an uncompensated expropriation their BIT's protection was enlivened.

(C) The proper measure

204. The above discussion suggests that further analysis is required to answer the central, deceptively simple question: what was the value of the "investment" destroyed?

205. This determination cannot be made by simple reference to the underlying value of the assets owned by Yukos. The Claimants were minority shareholders with exceedingly little power to make the policy decisions, such as dividends versus investment, that would enable them individually to access that underlying value. Their value was derived from those assets only in an indirect fashion, i.e. the prospect of dividends or share appreciation resulting from the corporate entity's successful exploitation of its assets. Those prospects could be affected, for better or worse, by factors such as the quality of Yukos' management, the effect of governmental economic policies of legislation, and obviously the vicissitudes of international markets.

206. One can therefore agree with Professor Ruback's basic premise that the value of a portfolio investment is simply given by the market. One can also agree with the Respondent's criticism of Professor Ruback's proposed understanding of what "the market" here means, since it involves both the selection of a reference date as being that of "the last reliable stock price" and projections as to the future market evolution.

207. Professor Ruback's putative "last reliable stock price", the Respondent argues, was necessarily arbitrary. There is force in this objection. True enough, 14 April 2004 was the day before an important event, but on what basis could it be concluded that the selection of this moment would purge the narrative of all improper conduct of the Respondent? Why not 8 December 2003, when the re-audit of Yukos' Y2000 began? Why not 25 October 2003, when Mr Khodorkovsky was arrested? Why not the much-discussed February 2003 meeting of oligarchs with Mr Putin in the Kremlin, which Mr Aron testified was the start of the personal "animosity" between him and Mr Khodorkovsky? (T:Day 3:73:16.) Would not early 2002 be the *safest* "reliable price", i.e. before the earliest of any arguable indications of Yukos being targeted by official antagonism?

208. These questions are far from idle, because the price of Yukos' shares was well below $10 as of the beginning of 2003. If one goes along with the $14 price as of 14 April 2004 notwithstanding the presumably adverse effects of Mr Khodorkovsky's travails and the gathering storm clouds of a major tax problem, need one infer that there had been some significant unrelated positive development which did much more than offset them? The present Tribunal has not in fact been presented with evidence of such a factor.

209. As for tracing a trajectory of the value of Yukos' shares but for the Respondent's conduct, one finds one's self in the familiar quandary of all who dream of predicting the future value of publicly traded shares. Of course Professor Ruback's analysis is not a projection into the *future*, because he wrote his opinions well after the date of his valuation (23 November 2007), but it is still a pure hypothesis, because it seeks to determine what would have happened in a *different past* than that of reality.

210. It takes no great macroeconomic insights to surmise that investors would have been attracted to a major oil company at a time of rising international prices, but this plausible assumption is hardly satisfactory as a basis for establishing the quantum of damages. Professor Ruback instead referred to a cohort of four of Yukos' Russian competitors (LUKoil, Surgutneftegas, Tatneft, and Bashneft). He established a ratio ("coefficient") between the returns of this cohort and those of Yukos over the two years preceding 14 April 2004, and then (to simplify) applied that ratio by comparison with the returns actually earned by the cohort from 14 April 2004 to 23 November 2007.

211. The conceptual construct is impressive, but as the Respondent points out involves a number of choices which are matters of judgment rather than science. For example, why a two-year period rather than any other length of time to establish the relative profitability coefficient? What is one to make of a major oil discovery by one of the cohorts in the post-14 April 2004 period;

does it not give the extrapolated Yukos "price" an unavoidable and undeserved boost? And what is to be inferred from the omission of a constant term, one of the "most obvious and widely used explanatory variables in asset return models," according to Professor Dow. (SoD ¶ 491.) The Respondent has ably articulated these objections to the Claimants' demonstration. The Claimants, for their part, recognize that the Tribunal may adjust Professor Ruback's model by subtracting any taxes that were legitimately owed by Yukos and any Yukos assets that were removed from Russia by Yukos' majority shareholders and managers. (SoRep ¶¶ 471-72.) (The Tribunal notes that the Respondent and its expert, Professor Dow, disagreed with the Claimants' suggestion.) The Claimants also acknowledge that the use of a constant term would decrease the predicted Yukos stock price on 23 November 2007 from $35.97 to $33.22 using a 2-year window or $17.67 using a 1-year window. (Second Expert Report of Professor Ruback, ¶ 12.)

212. These salvos cast doubt on the accuracy of the forecast which is at the core of the Claimants' quantum analysis. Yet the Respondent's presentation itself has a critical flaw: it does not set forth an alternative, more reliable forecast. The likely reason is obvious: while the very nature of Professor Ruback's approach leaves it open to challenges as to its *precision*, macroeconomic indicators make it overwhelmingly clear that the value of Yukos' shares would have substantially increased over the relevant time frame. The required certitude is not as to a precise number, but as to the reality of a substantial deprivation for which the wrongdoer cannot escape liability by insisting on its lack of detailed exactitude – and *a fortiori* when it presents no better alternative analysis.

213. Thus, there is no warrant to be dismissive of Professor Ruback's particular interest in Rosneft, which after having acquired a preponderance of Yukos' assets was transformed into a publicly traded company in 2006, and in connection therewith published an evaluation of its assets. By reference to that valuation, Professor Ruback

finds concordance with his projection of what should have been Yukos' share value on 23 November 2007. This is neither irrelevant nor unrealistic. Professor Dow, the Respondent's expert, testified very fairly that "sometimes the market gives different valuations to apparently quite similar assets inside different companies or even identical assets inside different companies." (T:Day 6:87:2.) This limited criticism in fact confirms that the comparison is of interest. It is a conventional wisdom of portfolio investors that they go to great length to establish the value of underlying assets as an indication of the true worth of investments, finding advantage in thus seeking to avoid the errors of perception and mood in the market.

214. There is nothing untoward about compensation that reflects a profit to the Claimants by reference to their price of acquisition. It is but the confirmation of compelling market realities. In the spring of 2003, the leading crude oil benchmarks reflected a price per barrel of around US$20. By the end of the year 2007, the number had shot up to $100. Half a year later, it had further increased to $160. Although it has subsequently fallen (and risen) over the intervening years, the US$20 benchmark seems of a distant age. In short, the year 2003 was a good year to have purchased shares in oil companies at an advantageously low price. It would thus also have been a good year for a state to expropriate an oil company, looking at the matter from the sole perspective of minimising the compensation. This the Respondent could have done by a plain and simple decree to that effect, duly motivated by governmental policy. Instead, it engaged in a series of measures over many months, resulting in the consummation of Yukos' dismantlement and effective expropriation at a time when the value of the Claimants' shareholdings had plainly appreciated. The Respondent suffers no loss by virtue of the present award, which comprises no element of a penalty for illegal expropriation, which is beyond the jurisdiction of the Tribunal (see Paragraph 45 above). The Respondent is simply ordered to pay for what it took, valued at the time of the taking, and without any consideration of the benefits it may since have enjoyed by reason of its actions

– whether in terms of pure revenue or in the achievement of policy objectives. The Tribunal recognizes that certain of the Claimants (i.e., Rovime and Quasar) purchased their shares prior to 15 April 2004, the day of the "threat" of expropriation, while the remaining Claimants (i.e., Orgor and GBI) purchased their shares after this date. But this does not mean that "[n]either Rovime/Quasar's failure to divest, nor Orgor/GBI's making of their purchases in the face of alleged expropriation, is compensable." (SoD ¶ 473.) The Tribunal finds instead that the Claimants "cannot be denied compensation for failing to predict Russia's expropriation of the company." (SoRep ¶ 462.)

215. In light of this discussion, it remains to attach a number to the claim. It is trite law that an international tribunal which has found liability and loss is not impeded from granting compensation only because the latter cannot be computed with certitude. One must simply admit that one does not know exactly what the Claimants' shareholding would have been worth had it not been destroyed by the compensable measures in this case, and then do one's best to make a fair assessment that does not penalise either side. (It is recalled that the claim is for simple uncompensated expropriation, not *unlawful* expropriation.) With the tools available to it, the Tribunal effects a downward adjustment of the claim which is intended to take into account the various challenges raised against the claims. It does so – all the while admitting that Professor Ruback's model may well have been validated by events but for the Respondent's actions – by replacing his $14 starting point (Yukos' share price on 14 April 2004) with $10.80 (Yukos' share price on 19 December 2003 when the Claimants made their first purchase), leading to a predicted Yukos share price of $27.76 as at 23 November 2007. This downward adjustment of approximately 23% does not claim to satisfy the rigours of corporate financial accounting; it does not, for instance, reassess Professor Ruback's "competitors' index" on the basis of the longer time frame thus established. But under the present circumstances, where the Respondent did not offer an alternative forecast and the Claimants recognized the Tribunal's authority to

adjust Professor Ruback's model, it is the Tribunal's view that this downward adjustment more properly represents the actual value of the Claimants' shares but for the Respondent's expropriatory measures.

216. The Tribunal, as alluded to above, rejects the Respondent's argument that Professor Ruback's valuation of Yukos is "speculative" because "[a]fter Claimants purchased their ADRs . . . the Yukos share price never went close to US$35.97." (SoD ¶ 492.) While it is true that the Yukos share price never increased to $35.97 (or $27.76, accounting for the Tribunal's downward adjustment), the reason is straightforward: the Respondent never gave Yukos the opportunity. The Tribunal refuses to ignore Professor Ruback's economic analysis simply because the Respondent's drawn out actions in expropriating Yukos suppressed the stock price, particularly when the Respondent failed to present an alternative valuation approach. Instead the Tribunal relies on Professor Ruback's model, while imposing a downward adjustment anchored on a fixed date (and corresponding Yukos stock price) in the record: 19 December 2003, when the Claimants made their first purchase of Yukos stock, at a price of $10.80.

217. To be clear, the Tribunal has not made a finding that 19 December 2003 is the date of the "last reliable stock price." Nor is 19 December 2003 the date that all of the Claimants purchased all of their Yukos shares. It is rather the date when the Yukos stock price was $10.80, which was approximately 23% lower than the $14.00 stock price on 14 April 2004. (Arguably the Tribunal could have selected 23 or 29 December 2003 when the Yukos stock price was also $10.80.) While this downward adjustment might lack precision, it is the Tribunal's view that under the present circumstances its approach adequately compensates the Claimants for the expropriation of their investments and avoids awarding a windfall.

218. Based on their respective holdings (the equivalents of their ADRs in ordinary shares); the Claimants' individual recovery is therefore as follows, at

Qasar de Valores SICAV S.A. (11,000 shares)	$305,360
Orgor de Valores SICAV S.A. (34,000 shares)	$943,840
GBI 9000. SICAV S.A. (18,000 shares)	$499,680
ALOS 34 S.L. (10,000 shares)	$277,600

219. The Respondent's final objection to the claim is that the quantum of recovery in this case must in any event be reduced by reference to the evidence of the Claimants' behaviour as investors, which was said to be focused upon speculation in distressed stock, with the investors manifestly willing to dispose of or reacquire their shares at a moment's notice (so-called "flipping"). Although there is evidence of some of the Claimants having gone in and out of a position in Yukos prior to purchasing the final contingent of shares which were rendered worthless by the extinction of Yukos, there is nothing about such investments – once made – that requires a different approach to the quantification of damages. In other words, once an investment qualifies for protection under the treaty (an issue upon which all Parties have previously made their submissions, and which was addressed in the Tribunal's Award on Preliminary Objections), there is no basis then to import some alternative method of quantification of damages, by reference to the assumed future intentions of the owners of the property rights in question. Shareholdings in corporate entities represent stakes in their assets and goodwill, valued by reference to the anticipation of income streams going into the indefinite future. The possibility that individual shareholders, for an infinite variety of reasons, may choose to trade their holdings

does not change the value of such rights for the time being, or the approach as a matter of law to the quantification of loss. Indeed, if anything, the liquidity of the assets in question, in and of itself, is likely to be a significant element in their value.

8. COSTS

220. The Claimants seek an award of costs in the overall amount of US$14,572,671.57. The Respondent asks for US$9,412,260.73. (The unusual proportionality between these claims and the claim on the merits – of some $2.6 million – is to be understood by reference to the circumstances described in Paragraphs 31-34 above).

221. The Claimants have, broadly, prevailed. One might look at isolated incidents in the arbitration in connection with which the Claimants were either unsuccessful or created unnecessary complications, and effect reductions on account thereof. Still, the overall result is a finding of liability and an order for compensation. Articles 43 and 44 of the SCC Rules, as well as Section 42 of the Swedish Arbitration Act 1999, provide support for the proposition that the prevailing party is entitled to recover costs incurred by it. The Claimants' petition for costs may thus be considered as advanced in the ordinary way.

222. But this is no ordinary case, since it is admittedly entirely financed by a third party, Menatep.

223. The usual arguments about the recoverability of costs where a party's participation in a case has been financed by a third party are inapposite here, because such third-party financing is typically part of a legally enforceable bargain under which the prevailing party in the arbitration has given up something in return for that support. Here, it is conceded that there is no legal duty on the part of the Claimants to hand over any recovery on account of costs to Menatep. The argument that the latter could successfully sue the Claimants in Spain under the theory of unjust enrichment does not lie comfortably in the mouth of the Claimants' own counsel, who in fact also acts for Menatep and indeed made it quite clear that while

the latter would be pleased to receive some recompense from the Claimants, this would depend on the latters' sense of moral obligation rather than a legal entitlement. Indeed the unjust enrichment argument is hopelessly circular; the duty to pay compensation cannot arise because the Claimants would incur an obligation if compensation were ordered.

224. The Respondent's position is this: "[The Claimants] have incurred no costs in this case. Stipulation from counsel: they don't have to pay a penny of any recovery to counsel or to Menatep. It is a total free ride." (T:Day 9:13:1-4.) This straightforward proposition must be right. On the one hand, the Claimants have neither expended money nor incurred obligations on account of the costs of pursuing their claims. On the other, Menatep, the Claimants' Good Samaritan (as it were), has no standing before this Tribunal or indeed more generally under the BIT.

225. The SCC has determined the costs of the arbitration as follows: Mr Paulsson, fee of EUR 400,000 and reimbursable expenses of EUR 17,483; Judge Brower, EUR 240,000 and EUR 13,216, respectively; Mr Landau, EUR 240,000 and EUR 6,830, respectively; SCC administrative fee, EUR 60,000. A party may bring an action against the determination of the fees of the arbitrators within three months from the date upon which it receives the award. Such action shall be brought before the District Court of Stockholm. The arbitrators have been informed that in view of the failure of the Respondent to provide the full half of the advance payments required to meet these costs, the advances made on behalf of the Claimants represent some 86% of the total, and that after payment of these costs there remains a credit of EUR 134,043. Seeking to maintain consistency, as far as possible, with the conclusion reached in Paragraph 224 with regard to the claim for direct costs, the arbitrators have decided, not without some reluctance given the Respondent's failure to meet what is in principle a joint duty to provide equal advances, not to order payment by the Respondent of the shortfall of its contribution. But

given that the Respondent has consented to these proceedings under the terms of the BIT, and given the outcome of the case, the arbitrators consider, in the exercise of their discretion, that the partial advance made by the Respondent shall be applied as a contribution to the costs of the arbitration as detailed above (since this amount will not be recovered by the Claimants, and since the arbitrators would consider it wholly improper to allocate the entirety of these costs to them as the prevailing parties), with the effect that the parties' liability for costs is allocated in the amounts of EUR 837 655 to the Claimants and EUR 139,874 to the Respondent, and that the credit balance shall remitted to the Claimants.

9. INTEREST

226. The Claimants seek pre-award interest on the sums awarded to them from 23 November 2007 until the date of this Award. The BIT is silent on the subject of interest. Nor do any of the provisions of Russian law relied upon by either side address this matter. In these circumstances, the Tribunal considers that the Claimants' position should prevail on the footing that the proper measure of compensation under general principles of international law should put them into the position they would have been in if there had been compliance with the BIT, that is to say compensation would have been paid to the Claimants upon the expropriation of Yukos and they would have been in a position to earn interest thereon. The Tribunal accepts that as a matter of realism this includes the compounding of interest; see John Gotanda, "A study on Interest", *VI Dossiers of the ICC Institute of World Business Law* 19-28 (2008) and authorities cited therein. The Respondent has not questioned the Claimants' assertion that as of 23 November 2007, Russian sovereign medium-term dealt in US Dollars had a yield of 6.434%. The date (which corresponds to the expurgation of Yukos from the Russian United Register of Companies) and the rate are therefore adopted by the Tribunal.

10. ORDER

227. For the reasons given above, the Tribunal hereby orders the Respondent to make the following immediate payments:

US$305,360 to Quasor de Valores SICAV S.A.

US$943,840 to Orgor de Valores SICAV S.A.

US$$499,680 to GBI 9000 SICAV S.A.

US$277,600 to ALOS 34 S.L.

228. Interest shall run on these four amounts at a rate of 6.434 % , compounded annually, from 23 November 2007 until the date of effective payment.

Done on the 20th day of July 2012.

Charles N Brower

Toby T Landau

Jan Paulsson