



CAREY OLSEN

## Piercing the 'corporate veil' – the Russian Federation and Yukos Oil, where Russian vodka rights have been seized.

Service area / [Corporate, Dispute Resolution and Litigation, Trusts and Private Wealth](#)

Legal jurisdiction / [Guernsey](#)

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John Greenfield, Guernsey senior partner, and Julia Schaefer, senior associate, were requested by the parties in dispute with the Russian Federation to give expert evidence on issues involving piercing the 'corporate veil' of companies and trusts against the factual background set out below. This evidence was put before the Court of Appeal of the Hague and resulted in a successful outcome leaving the Russian Federation facing a compensation/damages award of some US\$57 billion. Further appeal proceedings are anticipated.

### The proceedings

The proceedings before the arbitration tribunal were commenced by Hulley Enterprises Ltd ("HEL") (56.3%), Veteran Petroleum Ltd ("VPL") (11.6%), and Yukos Universal Ltd ("YUL") (2.6%) (together "HVY" or "the Claimants"), the three majority shareholders in Yukos Oil Limited ("Yukos"), the Russian oil company, for damages arising out of the actions taken by the Russian Federation against HVY and its beneficial owners.

HVY are arranged in what was described in the proceedings as the "HVY Holding Structure". It consisted of a standard-form structure of trusts and companies. HEL and YUL own 50.97% of the Yukos shares. HEL is wholly owned by YUL, and is itself owned by another company ("GML"). GML, in turn, is owned by seven Guernsey trusts, being trusts established in accordance with the laws of Guernsey, which for the most part hold their shares in GML via various nominee companies.

Yukos had been incorporated in 1993 following the dissolution of the Soviet Union, and later privatised as a vertically integrated group engaged in the full gamut of activities relating to the exploration and distribution of crude oil, natural gas and petroleum products.

HVY claimed that Yukos was bankrupted in 2006 owing to a "full assault" by the Russian Federation, which consisted of deliberate actions intended to destroy the Claimants' investment in the company for the government's sole benefit.

The alleged actions taken by the Russian Federation consisted, chiefly, of (1) deliberate and targeted onerous tax demands, which had as their primary objective to bankrupt Yukos and appropriate its assets, (2) a campaign of intimidation and harassment of Yukos personnel and advisers, and (3) the forced sale of Yukos' core production subsidiary by way of a rigged auction process in order to facilitate the acquisition of that subsidiary by Rosneft, a Russian State-owned company, for a price significant below market value.

In the initial proceedings in 2014, the UNCITRAL tribunal seated in The Hague, and consisting of three judges, unanimously ruled in HVY's favour, awarding the Claimants an unprecedented US\$50 billion in damages (consisting of interim awards made in 2009, and three final awards).

On appeal by the Russian Federation in 2016, the damages awards were overturned and set aside by the District Court of The Hague, which decided that in fact the arbitration tribunal did not have jurisdiction to hear the HVY claims.

HVY appealed that ruling, and following hearings in the summer of 2019, the Court of Appeal in The Hague overturned the District Court's decision, thereby reinstating the awards in favour of the Claimants. The Court of Appeal held that the provisional application of the Energy Charter Treaty ("ECT") did not violate Russian law, and that accordingly the tribunal had jurisdiction to hear the dispute under the ECT. It also rejected all other preliminary and substantive challenges advanced by

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the Russian Federation. This included the argument that the shareholders in Yukos did not qualify as “investors” pursuant to A. 1(7) ECT, because certain individuals involved with the shareholders were Russian citizens. The Court rejected this argument, on the basis that there was no legal principle of international law stating that investment treaties do not offer protection to entities controlled by a subject of the host country, nor that active economic contribution into the host country was required. HVY have seats of incorporation in countries other than the Russian Federation, and the fact that Russian citizens were involved in the companies and trusts comprising the structure was not material to prevent the application of the ECT.

## Carey Olsen’s involvement in the appeal proceedings

Carey Olsen’s involvement in the Appeal proceedings related to the central question of the application of A. 1(7) ECT, and whether the Court could and should look behind the HVY trust structures and to the ultimate beneficial owners by piercing HVY’s corporate veils to expose the individuals involved with the structures (some of whom are amongst the beneficiaries/settlers/protectors of the Guernsey trusts). The Russian Federation claimed that this, in turn, would show that the Claimants were in fact Russian citizens and therefore barred from making claims pursuant to the ECT.

Advocate John Greenfield’s expert opinion in support of the Appeal provided an analysis on the Guernsey law of piercing the corporate veil of companies, and demonstrated that it is not applicable to a Guernsey trust. As a result, it was not open to the Court to ‘look behind’ HVY’s seats of incorporation and towards any individuals involved with the structure. It provided a defence to the argument that the ECT was not applicable because of the involvement of Russian citizens in the structure.

Moreover, the Russian Federation had argued that the HVY structure was unusual and illegitimate, and therefore should be set aside as a ‘sham’. Advocate Greenfield’s opinion demonstrated that there was no evidence for that claim, and that the Royal Court of Guernsey would generally uphold legitimate corporate trust structures such as the HVY Holding Structure, requiring significant and compelling evidence to rebut any presumption of legitimacy. No such evidence had been put forward.

On the substantive question of Guernsey law in respect of piercing the corporate veil of a company, it is a long and well-established principle in Guernsey (and English) law that the fact that an individual owns and controls a company does not suffice to justify piercing the corporate veil<sup>1</sup>, and it is not justifiable for the court to pierce the corporate veil merely because this might be necessary in the interests of justice.<sup>2</sup>

The most recent exposition of the principles applicable in Guernsey is as set out by the Supreme Court of the United Kingdom in the leading case of *Prest v Petrodel* [2013] UKSC 34. This identified a distinction between the “concealment principle” and the “evasion principle”. While the former may lead to ‘lifting’ the veil of a company to look at what is behind it (without interfering with the corporate identity), the latter entails ‘piercing’ the corporate veil, i.e. disregarding the corporate identity to assign obligations of the company to those behind the company, such as its shareholders.

Contrary to the law on piercing the veil of companies, Advocate Greenfield’s opinion in support of HVY’s arguments identifies that Guernsey law does not regard a trust as a separate and self-standing legal entity, and instead trusts are sets of obligations operated by and via the trustee.<sup>3</sup>

The approach is necessarily different in relation to a trust than to a company, owing to the fundamental difference between the two underlying legal concepts. A company is a separate entity from its shareholders who, generally, have limited liability for its debts. A trust, on the other hand, is rather “a description of the obligations which the trustees owe to the beneficiaries for whom they hold the assets”<sup>4</sup>. These obligations would be enforced in the same manner as a contract, which in turn means that the concept of a ‘veil’ does not apply to a trust, just as it does not apply to a contractual relationship. Accordingly, there exists no cause of action of piercing the veil of a trust, even where a settlor has succeeded in assuming control of, and misused, a trust.<sup>5</sup>

Rather than ‘piercing’ through any structure, when it comes to trusts, the court can instead seek to determine whether the legal obligations per the trust deed are valid, or whether they are a sham. The decision is binary, and there is “no half way house between sham and validity”<sup>6</sup>. This approach is distinct from piercing the corporate veil of companies (i.e. the ‘evasion principle’). Where there is a valid deed of trust, assets will have been settled into trust, and are therefore no longer under the control and ownership of the settlor. Where it does not, the trust will be regarded as a sham, and the assets are deemed to be held on a resulting trust for the settlor by the trustees. In the HVY claim, there was no evidence that the trusts in the HVY Holding Structure were shams.

Such finding would have required the trust deeds themselves to be a sham, with a common intention by the settlor and trustee at the time of creating the trust that the true position between them should be otherwise than as set out in the trust deed, with an intention of both the settlor and trustee to mislead third parties or the court of those intentions.<sup>7</sup> Mere wrongdoing is not sufficient, and neither is constructive knowledge by the trustee of wrongdoing.

<sup>1</sup> *Salomon v Salomon & Co Limited* [1897] A.C. 22.

<sup>2</sup> *Trustor AB v Smallbone (No.2)* [2001] 1 W.L.R. 1177.

<sup>3</sup> *Grupo Torras S.A. and Culmer v Al Sabah and Four Others* [2003] JLR 188 (often better known as *In the matter of the Esteem Settlement*).

<sup>4</sup> *Ibid*, at [98].

<sup>5</sup> *Ibid*, at [518].

<sup>6</sup> *Ibid*, at [110].

<sup>7</sup> *Ibid*, at [110].

Continued

## Latest developments in the appeal proceedings

Russia has filed appeal proceedings before the Dutch Supreme Court, and reportedly a request has been made for the Supreme Court to refer questions of interpretation of the ECT to the Court of Justice of the European Union. Meanwhile, enforcement is – as always in litigation – a highly fought issue with surprising and interesting twists. Most recently, the Stolichnaya and Moskovskaya vodka trademark rights owned by the Russian Federation have been seized by the Claimants in partial satisfaction of the outstanding debt, which now runs at around \$US57billion due to additional penalty points.



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