

Russian Business Takes Legal Disputes Abroad

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May 05, 2015



While the political and economic challenges facing Russia are a continual concern, the fact that the country has not been able to establish a reputable legal system points to the difficulties it will face in its goal of becoming a major economic player.

Russia is now caught up in a vicious cycle, where companies conduct large transactions pursuant to foreign legal structures while the Russian legal and judicial system remains a relative backwater.

A recent case, *Neas Ltd, et al v. OJSC Rusnano, et al*, provides a vivid example of the outsourcing that has occurred since the demise of the Soviet Union.

Rusnano, an approximately \$2 billion Russian government-backed venture fund, is alleged to have illegally taken over Nitol, a former-Soviet-turned-private polycrystalline silicon producer in Siberia. Nitol is now owned by a corporation, which is organized under the laws of the Bailiwick of Jersey. Plaintiffs seek damages of not less than \$10 million.

While criminal charges are apparently pending in Russia relating to this affair, the plaintiffs have commenced a civil action in federal court in San Jose, California, through Rusnano's American subsidiary, Rusnano USA, which, the plaintiffs allege, is both the alter ego and the agent of Rusnano.

The complaint asserts numerous claims, including violations of the Racketeer Influenced and Corrupt Organizations Act, the California Business and Professions Code, and the laws of the Bailiwick of Jersey. The complaint makes no reference to Russian law.

The current saga began as a classic offshore structure for Russian transactions. Andrei Tretyakov, the former director of the Silicon Program for the Russian Federal Agency for Atomic Energy, formed a Cyprus company, Neas Ltd., through which to invest in Nitol, which in turn was owned by a Jersey company.

The twist is that after losing a takeover struggle with Rusnano, Tretyakov, who is now an American citizen living in Connecticut, is suing in a California federal court, where the Rusnano subsidiary is located, rather than through the British system with which Cyprus and Jersey are affiliated.

The outsourcing of Russian law began with the collapse of the Soviet Union in the early 1990s. Russian contract and company law was inadequate to support the massive redistribution of assets that arose when the Soviet Union collapsed.

Rather than upgrade the legal system, the Russian government opened the door for businesses to incorporate outside of Russia and enter into agreements governed by foreign law, often Anglo-Saxon law in England, Cyprus, Jersey, and Guernsey. Many major publicly traded Russian companies (such as LUKoil and Yandex) are organized in the Netherlands and the Dutch Antilles, jurisdictions that respect shareholder agreements that are governed by British law.

The Russian economic elites benefitted from immediate access to a sophisticated and largely respected Anglo-Saxon legal system and made little effort to reform the Russian legal and judicial system.

As a result, the massive asset redistribution of Russian natural resources that occurred after the collapse of the Soviet Union was structured to an astonishing degree outside of the Russian legal system. As of three years ago, 60 percent of the work of the London Commercial Court (a division of the High Court) has turned on Russian or other Eastern European disputes, often with no connection to England, according to David Christie, a London barrister.

One of the most famous disputes was a battle between two Russian oligarchs, ✕Boris Berezovsky and Roman Abramovich, in 2011-2012. The defendant, Abramovich, agreed to English jurisdiction, despite the lack of any English connection for the case at all.

In another 2012 case, involving aluminum kings Oleg Deripaska and Michael Cherney, the British court retained the case over Deripaska's objection, once again without any English connection at all.

There is some backlash. In the press, Britain has been criticized for “renting out” its legal system to companies and litigants who may have little link to England. And the British courts have refused jurisdiction on occasion.

For example, the English court refused in 2013 to accept jurisdiction of a breach of contract claim brought by Yelena Baturina, the wife of the former Moscow mayor, Yury Luzhkov. Baturina, residing in England tried to sue her Russian business partner, Alexander Chistyakov.

The English court dismissed the case, despite the fact that the agreement contained an English choice of law provision, because of the “overwhelming” links to Russia. However, in 2014, the Court of Appeal overturned this decision and returned the case to the London Commercial Court.

The impact of this failure of Russian law can be seen in an almost absurd fashion.

The Russian Venture Company (RVC), an approximately \$500 million fund that complements Rusnano’s more specific focus on nanotechnology, is required to structure its deals under Russian law.

Given that Russian law restricts shareholder agreements to such an extent that they more closely resemble contracts of adhesion than true agreements between sophisticated parties, this restriction to Russian law places RVC at a disadvantage to its private counterparts who remain free to outsource the law governing their deals.

In the Rusnano case described above, it remains to be seen whether the American reception will be as warm as that of the British.

At least one U.S. court has taken a hard line against federal cases brought by American citizens regarding foreign-based disputes. The court stated that when an American “chooses to invest in a foreign country and then complains of fraudulent acts occurring primarily in that country,” the power of American citizenship to act as a “talisman” against dismissal is diminished.

Indeed, one might ask why residents of Santa Clara County should be required to appear as jurors to determine the intricacies of a hostile takeover by a Russian company of a Russian plant in Russia.

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