



Pugachev convicted over funding of treaty claim

Sebastian Perry • Friday, 19 February 2016 (2 days ago)

Russian oligarch Sergei Pugachev has received a two-year prison sentence for contempt of court, with a UK judge ruling that a deal to fund his US\$12 billion investment treaty claim against Russia was in breach of a worldwide freezing order.



Sergei Pugachev (Credit: Wikimedia Commons)

The High Court in London sentenced Pugachev in absence on 12 February, a few days after finding him guilty of 12 counts of criminal contempt, one of which related to the arbitration.

The worldwide freezing order on £1.17 billion of Pugachev's assets was imposed by the High Court in 2014 in support of civil and criminal proceedings in Russia over his alleged role in the collapse of one of the country's largest banks, Mezhprombank, which he controlled before it was declared insolvent in 2010. A Russian civil court ruled last April that Pugachev caused the insolvency through fictitious lending to companies in his control and the oligarch's three appeals to the Russian Supreme Court have been dismissed.

Pugachev continues to deny any role in the bank's collapse and says he is the victim of a "witch hunt" resulting from Russian president Vladimir Putin's desire to expropriate his assets and destroy him.

In the latest proceeding, Mrs Justice Rose found that Pugachev had flouted the freezing order obtained by the bank and various other court directions by disposing of assets, making false submissions to the court and failing to hand over travel documents, personal devices and passwords. He had also left the country. She imposed the maximum sentence possible for contempt.

Rose J accepted that Pugachev had "a genuine fear that his life is in danger from agents of the Russian state" but said there was "no link between his fears for his safety and his decision to leave England".

She held that one of the ways he had breached the freezing order was by assigning part of the anticipated proceeds of his bilateral investment treaty claim to a New Zealand trust of which he is a beneficiary. Pugachev [filed the treaty claim](#) against Russia last November, seeking US\$12 billion in compensation for a "multi-pronged attack" on his family and his investments in the state's mining, shipbuilding, energy and real estate sectors.

Pugachev signed an agreement with the trust in July 2015, which provided that it would make a US\$800,000 upfront payment to King & Spalding – his counsel in the arbitration as well as in the English proceedings – and further "maintenance payments". In return, the trust would receive a portion of the proceeds of the BIT case, capped at US\$20 million. King & Spalding was not a party to the agreement.

The judge held the assignment amounted to a disposal of assets for which Pugachev had not sought the required consent of the bank or the court.

Pugachev was not in court but was cross-examined about the funding agreement via video-link. He claimed to have no recollection of signing it, even though his signature appeared on every page. Rose J refused to accept this, observing that Pugachev sees the BIT claim as "an important matter in his life" and "a way of refuting decisively the allegations made against him in the Russian proceedings [...] and of turning the tables on those who have tried to destroy him".

The judge also found that Pugachev was closely involved in changes to the governance of the trust that were carried out to ensure the funding agreement was concluded.

Pugachev argued that the assignment was not worthy of censure because there are currently no proceeds from the BIT claim, which is "very speculative". But the judge said this was irrelevant because the assignment became irrevocable on signing. She said Pugachev was well aware that the BIT claim was an asset in his possession and had previously disclosed it in a list of assets to the court.

The oligarch also argued that he was entitled to raise funds to cover legal expenses, and that the contempt of court proceeding was an attempt by the bank to frustrate the BIT claim. But Rose J said Pugachev could only use frozen assets to pay legal expenses in accordance with "important safeguards" set out in the freezing order. If the bank had refused to consent to the funding agreement, Pugachev could have argued before the court that the refusal was unreasonable – but it was not open to him to "sidestep" the court's order, she said.

In a letter to the judge before sentence was passed, Pugachev said he had entered into the funding agreement "in desperation and to keep King & Spalding as his lawyers". The judge said this would have had more mitigating force if he had answered questions about the agreement honestly.

However, Rose J accepted that the breach was "less serious" than Pugachev's disposal of other assets. She observed that King & Spalding had repaid the US\$800,000 it received to an account held by the trust, where it is now frozen by order of the court.

Another of the counts upheld against Pugachev was that he had breached the freezing order through his disposal of the proceeds from the sale of a French grocery business. More than €1.4 million of those proceeds were paid in legal fees to King & Spalding, with another €26,000 going to Latham & Watkins.

There was no allegation that either firm had acted in contempt and the judge did not say that the firms had behaved improperly in receiving payments from Pugachev.

A second freezing order remains in place

Pugachev's agreement to fund the BIT claim also comes under scrutiny in a separate [judgment](#) of the English High Court issued on 12 February by Mr Justice Mann. That proceeding considered a second freezing order that Mezhprombank obtained last August after learning that the trustees of five trusts linked to Pugachev had been replaced. Pugachev and his son had made the new appointments only three days before the funding agreement was concluded.

The second freezing order was against the replacement trustees, who were held to be under Pugachev's control and likely to dissipate assets on his behalf.

Rejecting the trustees' petition to lift the freezing order, Mann J said the "rushed timescale" in which the funding agreement was concluded created a "question-mark" over their independence.

Mann J said there was enough evidence to support the inference that the trustees were appointed because they would enter into the funding agreement, though he did not need to make a positive finding that they were under Pugachev's control.

The "independence and care" of the trustees was called into question by the fact that the funding agreement on its face represented a breach of the first freezing order, Mann J said.

He noted that the trustees had also breached the second freezing order when they made the initial payment of US\$800,000 to King & Spalding without first disclosing it to the bank. This suggested they were "very keen" to enter into the transaction.

Taken together, the judge said the structure of the trusts, Pugachev's alleged propensity to conceal assets, the change of trustees and their subsequent conduct all pointed towards the oligarch's "de facto" control of the trusts.

Looking behind trusts' ownership structures

King & Spalding is no longer acting for Pugachev in the English proceedings, having won permission from the court last month to withdraw as counsel. The firm declined to comment on the latest High Court rulings.

It remains unclear whether King & Spalding will continue to act in the arbitration, or whether Russia has instructed external counsel for the dispute. GAR understands that the case has not progressed since the filing of the claim last year, as Pugachev has yet to appoint an arbitrator.

Hogan Lovells has been acting for Mezhprombank and its liquidator in the English courts but is not involved in the arbitration. Michael Roberts, an investigations partner in the firm's London office who is leading work on the case, says Pugachev has been found guilty of "a staggering and quite possibly unprecedented number and range of allegations of contempt of court".

He calls the sentence "an important step forward" in the efforts of Mezhprombank's liquidator to recover Pugachev's assets for the bank's creditors.

Roberts adds, "The trusts aspects of the litigation are particularly groundbreaking and demonstrate the flexibility of the English court in ensuring that its orders cannot be frustrated by complex ownership structures."

Mishcon de Reya is acting for the trustees in the English courts.

Pugachev was recently [interviewed](#) by the BBC's Panorama for a programme entitled "Putin's Secret Riches", exploring allegations that the Russian president has used his power to amass a large personal fortune, which Putin denies.

[JSC Mezhdunarodniy Promyshlenniy Bank & Anor v Pugachev \[2016\] EWHC 192 \(Ch\) \(08 February 2016\)](#)

[JSC Mezhdunarodniy Promyshlenniy Bank v Pugachev \[2016\] EWHC 258 \(Ch\) \(12 February 2016\)](#)

High Court bench

- Mrs Justice Rose

Counsel to Mezhprombank and Deposit Insurance Agency

- Stephen Smith QC, Ben Griffiths and Anna Scharnetzky of Erskine Chambers
- Hogan Lovells

Partners Michael Roberts, Rebecca Wales and Chris Hardman in London and Alexei Dudko in Moscow

Counsel to Sergei Pugachev

- King & Spalding (until 27 January 2016)

Stuart Isaacs QC, Nicholas Cherryman and Moeiz Farhan in London

JSC Mezhdunarodniy Promyshlenniy Bank & Anor v Pugachev & Ors [2016] EWHC 248 (Ch) (12 February 2016)

High Court bench

- **Mr Justice Mann**

Counsel to Mezhprombank and the Deposit Insurance Agency

- **James Potts QC** and **Ben Griffiths** of Erskine Chambers
- Hogan Lovells

Partners Michael Roberts and Rebecca Wales in London and Alexei Dudko in Moscow

Counsel to Sergei Pugachev, Kea Trust, Finetree, Bramerton, Bluering, Maru, Hapori, Miharo, Arotau, Luxury

Consulting and Victor Pugachev

- **Stephen Auld QC** and **Rachel Oakeshott** of One Essex Court
- Mishcon de Reya

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