



## The Yukos Chapter 15 Case:

### The story of how a United States Bankruptcy Court's pragmatic approach to a novel problem aided a Russian receiver to protect assets located in the Netherlands



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Chapter 15 of the United States Bankruptcy Code permits a bankruptcy court to grant recognition to a foreign bankruptcy case. Chapter 15 also permits the bankruptcy court to enter orders that are “urgently needed to protect the assets of the debtor or the interests of the creditors.” In the recent case of Yukos Oil Company, one of the first cases under Chapter 15, the bankruptcy court was faced with a request by a Russian receiver (represented by Chadbourne & Parke LLP) for the enforcement of a Russian order prohibiting Yukos’s management from disposing of assets located in the Netherlands. Yukos and its major shareholder objected to the request on numerous grounds. The bankruptcy court carefully considered the purpose and objectives of Chapter 15, including the promotion of cooperation among courts of the United States and the courts of other foreign countries, in encouraging the parties to reach a consensual resolution that would ensure fair treatment of not only creditors in Russia, but also creditors in the Netherlands.

#### The Russian Proceeding and the Temporary Restraining Order

In May 2006, a consortium of banks filed a bankruptcy petition against Yukos with a commercial court in Russia. The Russian court placed Yukos under “supervision” and appointed an interim receiver. While in “supervision,” a preliminary and temporary stage of a Russian bankruptcy proceeding, a debtor’s activities are significantly restricted. The Russian interim receiver is responsible for, among other things, preserving the debtor’s property and taking measures to secure the debtor’s assets. In furtherance of his statutory obligation to preserve Yukos’s assets, the interim receiver sought and obtained “additional protective measures” in the form of an order from the Russian court enjoining Yukos and its management from entering into certain transactions or transferring Yukos’s property without the interim receiver’s consent.

Yukos has significant assets located outside of Russia, including a substantial stake, through its Dutch subsidiaries, in AB Mazeikiu Nafta, a company which owns a refinery in Lithuania. Prior to Yukos’s bankruptcy case, Yukos’s management team, consisting of several United States citizens or residents, was negotiating the sale of Yukos’s interest in Mazeikiu Nafta.

In furtherance of his duties, the interim receiver requested information regarding the Mazeikiu Nafta sale from Yukos’s management. Management ignored the interim receiver’s request for information and, notwithstanding the terms of the Russian court’s order, continued their efforts to sell this valuable asset of Yukos without the interim receiver’s consent.

In light of the lack of cooperation from Yukos and the interim receiver’s obligation to preserve Yukos’s assets for the benefit of the estate, the interim receiver commenced a Chapter 15

case and requested a temporary restraining order implementing the Russian court’s order in the United States. As discussed below, the bankruptcy court entered a temporary restraining order pursuant to section 1519 of the Bankruptcy Code. The temporary restraining order, consistent with the terms of the Russian court’s order, enjoined Yukos and its management from entering into certain transactions for the sale or disposition

of Yukos’s property without the interim receiver’s consent.

#### The Dutch Proceedings

Prior to the commencement of Yukos’s Russian bankruptcy, some of Yukos’s creditors had obtained attachments in the Netherlands over shares of stock of Yukos’s subsidiaries, including the subsidiary that ultimately held the shares in Mazeikiu Nafta. As a result, creditors holding attachments would be entitled to shares in Mazeikiu Nafta. Other creditors, including those that asserted claims in the Russian bankruptcy, would not have any rights to such proceeds unless they filed similar attachments in accordance with Dutch law. Accordingly, certain creditors holding attachments would be preferred over other creditors that did not hold attachments in the Dutch proceedings.

#### The Bankruptcy Court’s Reaction to the Chapter 15 Petition

Similar to ancillary proceedings under former section 304 of the Bankruptcy Code, an important objective in a Chapter 15 case is the entry of an order granting recognition to the foreign proceeding. Indeed, under Chapter 15, a petition for recognition “shall be decided upon at the earliest possible time.” However, unlike section 304, Chapter 15 divides foreign proceedings into foreign main and foreign nonmain proceedings. A foreign main proceeding is defined as a proceeding pending where the debtor has the center of its main interests, which is presumed to be the company’s

*“Prior to recognition, the bankruptcy court protected a valuable asset for the benefit of all creditors by adopting a pragmatic approach permitted under Chapter 15.”*

## The Yukos Chapter 15 Case (cont)

registered office. A foreign nonmain proceeding is defined as a foreign proceeding where the debtor has an establishment (i.e., a place of operations where the debtor carries out nontransitory economic activity). Recognition of a foreign nonmain proceeding does not result in automatic relief. On the other hand, upon recognition of a foreign main proceeding, creditors are automatically enjoined from pursuing collection efforts against the debtor.

Chapter 15 does make provision for the bankruptcy court to provide relief even before formal recognition, whether as a foreign main or nonmain proceeding. Section 1519 of the Bankruptcy Code authorizes a bankruptcy court to grant temporary relief upon the filing of a Chapter 15 petition “where relief is urgently needed to protect assets of the debtor or interests of the creditors.” According to the legislative history, section 1519 does not expand or reduce the scope of the bankruptcy court’s equitable powers, but rather ensures that a bankruptcy court will have jurisdiction to grant emergency relief, including injunctions, prior to recognition. Based on section 1519, the Petitioner requested provisional relief.

The bankruptcy court acted quickly and prevented the depletion of assets by issuing the temporary restraining order on an ex parte basis immediately after the Chapter 15 petition was filed. The bankruptcy court’s restraining order maintained the status quo and afforded the interim receiver an opportunity to consider the terms of the proposed sale of Mazeikiu Nafta. The temporary restraining order as initially entered imposed an absolute ban on Yukos’s participation in any discussions regarding the sale. Subsequently, with the bankruptcy court’s encouragement, Yukos agreed to provide the interim receiver with information concerning the sale and, in exchange, the interim receiver agreed to permit Yukos to resume negotiations of (but not consummate) a sale of Mazeikiu Nafta.

After due diligence and the receipt of information from Yukos’s management and advisors, the interim receiver concluded that the sale price (over \$1.4 billion) for Yukos’s interest in Mazeikiu Nafta was reasonable. However, the interim receiver refused to grant his consent to the sale given concerns about the transaction and that the only creditors that could share in the sale proceeds were those with valid attachments in the Netherlands. Russian creditors with valid claims who failed to obtain attachments in the Netherlands would not be able to share in the proceeds of the sale.

Given the interim receiver’s refusal to consent to the sale, the bankruptcy court faced a difficult choice. It could (i) enjoin the sale until such time as sufficient safeguards could be implemented to preserve the sale proceeds for the benefit of all creditors and run the risk that the potential buyer would walk away from the proposed transaction and Mazeikiu Nafta would later sell at a substantially lower price, or (ii) allow the sale to proceed without such safeguards. Ultimately, the bankruptcy court determined that the risk to Yukos of not consummating the transaction outweighed the interim receiver’s concerns. The bankruptcy court, however, in dissolving the temporary restraining order, urged the parties to resolve the issues regarding the treatment of the proceeds from the sale of Mazeikiu Nafta.

The parties ultimately agreed to the terms of a consensual order that was entered by the bankruptcy court. The order requires that the parties cooperate and take steps in the Netherlands to ensure that: (i) certain attachments are released, and (ii) all creditors have the ability to seek to share in the proceeds from the Mazeikiu Nafta sale. In order to accomplish this result, the bankruptcy court made certain requests and recommendations to the Dutch Court, including that, consistent with Dutch law, the Dutch Court implement a reasonable claims resolution procedure to ensure that all creditors have a fair opportunity to file claims and other parties have the right to object to claims in the Dutch Proceedings. In particular, the bankruptcy court requested that the Dutch Court, when considering a claim, first determine whether it should be allowed in the Netherlands under principles of comity and thereafter consider any substantive objection. The proceedings in the Dutch Courts are ongoing.

### Conclusion

Chapter 15 of the Bankruptcy Code provides a bankruptcy court with a great deal of flexibility in assisting foreign courts and trustees or other foreign representatives. While recognition is a key goal in a Chapter 15 case, a bankruptcy court may grant relief prior to recognition if warranted. In the Yukos Chapter 15 case, the bankruptcy court exercised a considerable amount of discretion in fashioning such relief. Prior to recognition, the bankruptcy court protected a valuable asset for the benefit of all creditors by adopting a pragmatic approach permitted under Chapter 15. Moreover, it did so in a manner that was incorporated into an order in the form of a request or recommendation to the Dutch Court. Future Chapter 15 cases may also involve similar recommendations or communications between courts.



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