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**INSTITUTIONAL CHANGE IN  
RUSSIAN CORPORATE  
GOVERNANCE:  
AN ANALYSIS  
OF CORPORATE DISPUTES**

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PhD

2008

# INSTITUTIONAL CHANGE IN RUSSIAN CORPORATE GOVERNANCE: AN ANALYSIS OF CORPORATE DISPUTES

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A thesis submitted in partial fulfilment  
of the requirements of the  
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## **ABSTRACT**

Russia has been lagging behind most of the developed countries and some of the transition economies in terms of the corporate governance infrastructure (Woodruff, 2004). However, the challenge to develop strategic assets, particularly in the form of oil and gas reserves, produced the need to attract foreign capital and expertise. This in turn has led to a mounting pressure to improve fundamental characteristics of corporate governance such as the regulatory environment, enforcement mechanisms, corporate structure and transparency (Preobragenskaya, 2004). Since strategic assets are at the very heart of the still undiversified Russian economy, it is easy to see how corporate governance has become one of the top priorities on the agenda of national reforms (EU-Russia Roundtable on Corporate Governance, 2006). This study attempts to register the perceived change in the institutional context in Russia through analysing reported corporate disputes. Thematic template analysis is applied to the data on corporate conflicts taken from the English language Russian press. The results of the study suggest a positive change in perception about the role of formal institutions with reference to private entities and a negative change in terms of perception in relation to state entities. This conclusion is based on the comparison of corporate disputes and enforcement practices employed by the parties to corporate disputes reported in 1998 and 2006. On an academic level this study addresses a call in the literature to give more consideration to the particularities of the management environment and the fragility of its social systems in Russia (Kuznetsov & Kuznetsova, 2001) as well as complement understanding of Russian corporate governance by concentrating on the in-depth analysis of company behaviour (Iwasaki, 2007).

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## DECLARATION

I declare that the work contained in this thesis has not been submitted for any other award and that it is all my own work.

Name: Roman Stepanov

Signature:

Date: 17/10/08

## CHAPTER 1: INTRODUCTION

### 1.1 Setting the Scene

In academic terms the subject of corporate governance has been intensively researched, particularly in the last two decades. A lot of research has taken place in the Anglo-Saxon, European and South East Asian contexts because of the economic influence of these regions. However, since the beginning of the transition from command to market economy, scholars turned their attention to Russia. The magnitude of the undertaken change made the country a unique laboratory for testing the robustness of market institutions. Western academics (Andrei Shleifer<sup>1</sup> and Bernard Black<sup>2</sup>) and finance providers (IMF, World Bank) conducted their experiments often not knowing what the result of proposed reforms would be. Since then, two opposing opinions were formed. The first opinion led by Shleifer (2005) defended the core of the transition and justified the reforms arguing that Russia became a 'normal country'. The second group of academics led by Black (2000) remained pessimistic about the very foundation of Russia's capitalism and directed their research efforts at explaining 'what went wrong'. Both camps produced highly insightful academic studies in support of their opposing opinions. Under such circumstances an academic truce can only be achieved by celebrating the complexity of the task at hand.

---

<sup>1</sup> Andrei Shleifer (Harvard Business School) was one of the key privatisation advisers in the earlier stages of Russia's transition.

<sup>2</sup> Bernard Black (University of Texas) led the development of the Russian law on Joint Stock Companies, 1996.

## 1.2 Brief Historical Background of Russia's Transition

The Russian socialist experiment ended because it produced a low standard of living for the majority of Soviet people; crisis of the single party system was profound; extreme militarization of the economy could not be sustained; difficult interethnic relations were exacerbating; and the central planning system was suffering from unprecedented levels of inefficiency. All of these factors led to a systemic economic and political crisis. The communist regime in Russia had no reserve capacity to outlive the crisis particularly exacerbated by the falling global oil prices (the last line of economic defence previously relied upon by the regime). The sentiment in favour of the radical regime change was felt strongly among Russian population which by the late 1980s began to realise and understand many of the deficiencies of the system. That sentiment was very much shared by 'the West' which saw communism as a significant threat to the free market ideology and hence was prepared to allocate substantial resources to the task of changing the Soviet system irrevocably.

No nation had ever attempted a transition from central planning to market economy on such a large scale<sup>3</sup>. Hence, those who happened to be in charge of determining the future of Russia's transition had little idea as to the impact of the contemplated reforms on the country and its economy. Nevertheless, the consultation process had to be quick because the reformers and their western advisors were fearful that the 'window opportunity' (Aslund, 1995, p.1) will close and the communists will re-gain their power grip over the country. Decisive action was required without delay.

Gorbachev was a proponent of a gradual change. The basic idea here was to retain the Soviet corporate infrastructure, but gradually reform sections of the economy aligning it more and more with the capitalist model. This is of course a reasonable approach to the task of steering the economy through the transition of an unprecedented scale. However, politically Gorbachev was in a very difficult position. The general mood of the public was biased against the communist party

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<sup>3</sup> The radical nature of the changes undergone are analysed in Aslund (1995), a western advisor directly involved in the reform process.



member when he was talking about gradualism. The mood on the streets, in the parliament (Duma), on television, at schools, in universities and at work was to change things radically. The more radical the proposed reforms, the more short-term support the reformers were bound to get from the population and the West who long wished the demise of the old regime.

Based on the above set of circumstances it is not surprising that Russia, in contrast with Czech Republic and Poland, opted for a speedy privatisation without giving much thought to what might happen as a consequence of turning the whole country into shareholders almost overnight. Nevertheless, in the space of months (rather than years or even better decades) 6,477 joint stock companies were registered. Between 1992 and 1993 privatization vouchers were made available to 150 million Russian citizens (Boycko & Shleifer, 1993).

Some argued that the reformers must have known that the experiment with private property of this magnitude was destined to fail in the absence of even the most basic market institutions (Black *et al.*, 2000) and culture. The country of shareholders did not have a single mechanism of addressing the massive agency problem that the reformers hastily created when vouchers (in essence shares) in Russian industrial assets were distributed among the general population.

It has been argued that it was only logical that the country turned into a criminal haven. Then, it was not unusual for the most valuable assets to change hands at one thousandth of their real value (Boycko & Shleifer, 1993). Ordinary shareholders saw their wealth expropriated by means of schemes involving the crudest forms of transfer pricing and asset stripping in the best cases and physical violence in the worst examples. Under such conditions, the quality of the evolving ownership class left much to be desired. The compromise that the reformers ultimately accepted meant that the subsequent stages of Russia's transition had to continuously account for the corrupt nature of the post privatization environment and consequently (or as a cause of corrupt privatization) a highly deficient ownership class (see appendix 10 for a list of Russian Oligarchs).

### 1.3 Rationale for the Study

The task of developing Russian corporate governance in line with ‘Western’ approaches has been growing in relevance as more and more companies in Russia seek to raise finance on foreign capital markets. In relation to the UK, the issue has become pertinent with a considerable increase in the number of Initial Public Offerings of large Russian enterprises on the London Stock Exchange (EU-Russia Roundtable, 2006).

However, meaningful investigations of corporate governance practices in Russia have been hindered by difficulties associated with gaining sufficient access to enterprise data and a general lack of transparency (Fox & Heller, 2000). Consequently, most studies attempted to avoid company-specific investigations by examining corporate governance on the macro level. Studies of this nature tend to investigate the development of corporate governance mechanisms, concluding with the implications for the companies operating in the environment. In the Russian context researchers conducted numerous investigations that attempt to assess the impact of various types of ownership, remuneration practices, board structures and levels of disclosure on corporate performance (Iwasaki, 2007). These typically positivistic studies often arrive at contradictory conclusions and rarely demonstrate a strong correlation between a certain corporate governance characteristic and firm performance. This study however, attempts to contribute to the body of knowledge by adding to the understanding of how companies operating in Russia responded to the efforts directed at changing the institutional<sup>4</sup> environment and corporate governance in the country. This research places emphasis on the actual company practice as opposed to a reform-driven analysis of the institutional context.

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<sup>4</sup> We use a standard definition of “institutions as rules and procedures (both formal and informal) that structure social interaction by constraining and enabling actors’ behaviour” (Helmke & Levitsky, 2004, pp. 727).

## 1.4 Summary of Contribution to Literature

With reference to studies of corporate governance in the Russian context, a great deal of emphasis has been placed on empirical research. A number of comprehensive surveys of the discipline in the Eastern European context (Djankov, 2002) and more specifically with reference to Russia (Iwasaki, 2007) call for more qualitative and multi-faceted approaches to studying the subject of corporate governance. The current study addresses this general gap in the literature by analysing reported corporate disputes and methods of their resolution as key determinants of the change taking place with reference to Russian corporate environment. In doing so, the study additionally contributes to the literature on the role of media in shaping corporate governance environment.

More specifically, the trajectory of the development of Russian corporate governance institutions has been debated by a number of academics. There is no agreement in contemporary literature on whether formal institutions are becoming an effective mechanism of overseeing corporate environment. Some conclude that moderate improvements have been achieved (Roberts, 2004), while others emphasise great inefficiencies of the legal system and the lack of the rule of law (Kochetygova *et al.*, 2004). This study directly contributes to this academic debate by studying the dynamics of the dispute resolution process in the country.

## 1.5 Objectives of the Study

In order to address the research question, the following objectives have been formulated:

- To review the literature on corporate governance in the Russian context, present definitions of corporate disputes and enforcement practices and discuss the role of media in the context of the clearly defined research question (Chapter 2);
- To select and justify a method of data collection and analysis that would most effectively address the research question. (Chapter 3);
- To examine the extent of media coverage of corporate disputes in 1998 and 2006 (Chapter 4, section 1);
- To analyse the nature of reported corporate disputes and methods of their resolution in the two years of the study (Chapters 4, sections 2, 3 and 4);
- To triangulate the data by interviewing reporters (Chapter 4, section 5);
- To examine forces that stimulate and prevent the development of corporate governance institutions in Russia (Chapter 5);
- To reach conclusions about the institutional change in the country based on the analysis of corporate disputes and methods of their resolution as well as analyse limitations of the study and propose further research (Chapters 5).

## 1.6 Research Question

In relation to transition economies, the development of greater investor protection, increased market control, a shift towards the rule of adequate laws and a more sophisticated judiciary are all complex processes which individually and as a whole are not subject to a single reform. The complexity arises from a great variety of both dynamic and inert factors at work. Looking for a relationship between a narrowly defined development and the trend in institutional dynamics is unlikely to produce meaningful results for that very reason.

In order to contribute to the understanding of the institutional development in Russia, the following two factors are proposed for consideration:

1. Reported conflicts and methods of their resolution at the beginning of transition
2. Reported conflicts and methods of their resolution in the modern environment

The reason for choosing reported corporate conflicts as a unit of analysis is twofold: firstly, there is an underlying assumption that reported material relatively accurately mirrors the actual environment (Dyck et al., 2008) and secondly, any system of governance is best tested by its exposure to situations with opposing interests and claims (Fox & Heller, 2000). The key research question here is:

- *What is the change in foreign investor perception about the institutional dynamics in Russian corporate governance based on the comparison of corporate disputes pertaining to two different time periods of Russia's transition?*

In the context of the above question, the term corporate dispute is defined as a conflict of interests among identifiable stakeholders which is usually (but not necessarily) followed by a resolution process.

## 1.7 Methodology

This study is conducted from the philosophical stance of pragmatism. It is a predominantly qualitative piece of research with a limited quantitative dimension. Current investigation is informed by case studies of corporate disputes taken from the archival material of the Moscow Times. The data on corporate disputes covers two years, 1998 and 2006 and is analysed using the method termed thematic template analysis (King, 1998). Additionally, semi-structured interviews are conducted with 5 reporters of the newspaper in order to complement and triangulate the data. Collected data is coded and categorized relative to the nature of corporate conflicts and enforcement strategies.

## 1.8 Structure of the Thesis

The thesis consists of 6 chapters namely, introduction, literature review, methodology, data analysis, findings and discussion and conclusion. All chapters begin with an introduction and are concluded with a brief summary of the main points.

**The literature review** chapter consist of three sections. The first section outlines the subject of corporate governance in general and in Russia. Moreover, the institutional context in the country is also discussed. The second section deals with the definition of corporate disputes and enforcement practices while the last section explains the role of the media in the context of this study. Each section is concluded with further clarification of the research question. Finally, an outline of the gap in the literature is provided.

**The methodology** chapter outlines the philosophical perspective, methodology and main method of data collection as well as analysis. Additionally, the chapter presents an outline of original contribution and methodological limitations of the study.

**The data analysis** chapter is divided into five sections. It is the largest and most prominent chapter of the thesis. The first section provides a numerical overview of the data set; the second, third and fourth sections present an analysis of the content of reported corporate disputes while the final section contains an analysis of the interview material.

**The findings and discussion** chapter presents the key drivers behind institutional change in Russia and original contribution of the study.

**The conclusion** chapter revisits the research objectives, discusses limitations of the study and provides suggestions for further research in the area.

## CHAPTER 2: LITERATURE REVIEW

### Introduction

This chapter is divided into three sections. The first section provides an overview of the subject of corporate governance in general and, more specifically, with reference to Russia. Corporate governance is discussed in the context of agency theory. The section also includes a description of the institutional context in the country outlining major forces behind the change. Here, the relationship between formal and informal institutions is described. The second section defines corporate disputes, and presents the literature on enforcement practices in the country. This section introduces *a priori* themes that are used at the stage of data analysis. The last section of the literature review discusses the effects of media coverage on corporate governance. Here, the link to agency theory is maintained through considering reputational costs of disputes/violations.

Each section is concluded with a refinement of the research question of this study. Finally, an outline of the key areas of literature to which this research contributes to will be presented.



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## Section 1: Corporate Governance and Russia

This section outlines the subject of corporate governance, provides a theoretical underpinning of the study and discusses the institutional context in Russia.

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### 1.1 Subject of Corporate Governance

In its all-encompassing sense, corporate governance is a discipline which is concerned with the way companies are managed. In the Anglo-Saxon context, there has been a particular focus on public companies where ownership and control are separate. Agency theory (Jensen & Meckling, 1976) is the core theoretical underpinning that provides the context/framework within which relationships between those who delegate (principals) and those who manage (agents) need to be considered.

In the context of a commercial public entity, managers are the agents and shareholders are the principals. The theory assumes self-centred actions of the agents and warns about the agency costs that inevitably arise when management are left unsupervised. In this context, the role of corporate governance is more narrowly defined and manifests itself through various control mechanisms that shareholders need to put in place in order to protect their interests and ensure that the profit-maximisation agenda is followed. Board composition, disclosure, remuneration policies, accountability, internal and external audits are all control mechanisms that seek to reduce the agency costs by both minimising the extent of insider dealing (managers acting in self-interest) and encouraging profit-maximisation.

The regulatory core of corporate governance is in the fiduciary duty of directors to act in the interests of shareholders. In the Anglo-Saxon context, this concept has been around for some time. However, fiduciary duty is not a straightforward regulatory concept. It requires a sophisticated institutional infrastructure, particularly when it comes to arbitration. The concept of fiduciary duty is difficult to enforce because of its complexity which arises from the deliberately loose or non-prescriptive legal underpinning.

Below is the discussion of the role of corporate law and formal institutions in achieving the desired effect of shareholder-oriented corporate governance<sup>5</sup>.

## 1.2 The Role of Legislation

The design of corporate law as a concept will depend upon its role within the business context. Varying national factors determine the role and hence the nature of the legal provisions (Black *et al.*, 1999).

The primary role of corporate legislation in developed economies such as Great Britain is to facilitate the business process. Here, company law and its reform are designed in such a way as to assist the decision making process aimed at wealth maximization, which is indeed the principal goal of corporate legislation (Black & Kraakman, 1996). The law acts in unison with supporting institutions that oversee the management and typically reacts to the anomaly of expropriation and/or management malfunction (Black & Kraakman, 1996). This fact allows a greater level of flexibility in the way a public organisation is run. Ideally, good managers need a complete decision-making freedom in their pursuit of wealth maximization as some restrictions might prevent profitable deals from taking place. On the other hand, investors require a certain level of protection which will minimize the risk of misappropriation and bad practice (figure 2.1). In developed economies, this role of legislation is supported by the effects of competition, relatively efficient stock markets, and a developed accounting profession, together with enforceable and clear rules against expropriation (Avilov, *et al.*, 1999). All of these result in a reasonably developed management culture which, coupled with informed investor expectations, lead to a relatively healthy business environment<sup>6</sup>. Therefore, most compulsory provisions are redundant, and those which are necessary tend to be in

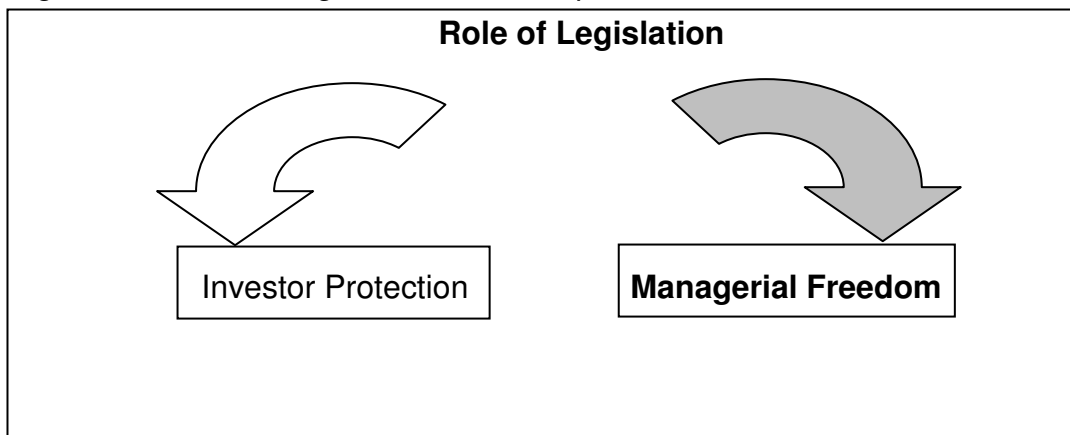
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<sup>5</sup> The stakeholder approach to corporate governance is not discussed, because it is argued, that in the Russian context of barbarian capitalism, as depicted by Freeland (2000), managers and oligarchs are not driven by anything other than self-interest. Moreover, Russia's transition produced enough confusion in the minds of indigenous managers and newly established owners, that an additional complexity associated with balancing stakeholder needs is simply prohibitive. Indeed, most academic studies of Russia's transition (Shleifer & Treisman, 2005; Mueller, 2006; Black, Kraakman, & Tarassova, 2000) consider corporate governance from the Anglo-Saxon perspective.

<sup>6</sup> That is not to say that the system is 100% protected from corporate scandals which continue to affect even the most developed economies.

line with what is usual and most logical practice anyway. Furthermore, courts have a sufficient level of expertise and enforcement capabilities to apply the concept of fiduciary duty as a measure against blatant cases of managerial misconduct (Black *et al.*, 1999). Whatever is in the grey area of managerial practice and does not fall into the 'bright line' category of corporate misconduct, is left for the markets to interpret. The process is facilitated by a number of mechanisms that seek to protect the interests of shareholders (principals) against self-centred motives of the management (agents). In developed economies this structure, although not faultless, more often achieves the required balance of power to the mutual benefit of those who provide the finance and those who manage the business.

Figure 2.1: *Role of Legislation in Developed Economies*



### 1.3 Corporate Governance in Russia

Since the break-up of the Soviet Union, Russia has been struggling to create a sufficiently robust institutional infrastructure. The country's transition from command to free-market economy did not produce the results most reformers had hoped for. Endemic corruption that paralysed the efforts to reform the economy is the most commonly cited reason behind the failure (Black *et al.*, 2000; Black *et al.*, 2002; Levin & Satarov, 2000; Roaf, 2000). There is no consensus among academics as to what caused such unprecedented levels of corruption.

Some blamed the ‘shock therapy’<sup>7</sup> strategy of privatising national assets (Black, 2002; Ellerman, 2001) admitting that the input of Western advisors was counterproductive. Yet others defend the credibility of ‘shock therapy’ explaining the rise in corruption as an inevitable side effect of such a dramatic transition (Shleifer & Treisman, 2005).

Whatever the underlining reasons, the privatisation chapter of the Russian transition was closed (at least temporarily) by numerous reassurances coming from president Putin that there would not be any centralised efforts to review/reallocate existing property rights at a national level. The significant shareholding structures in Russia appear to be more stable with the exception of a number of politically motivated instances of de facto re-nationalisation. It could be argued that Russia has paid the price for changing its regime by surrendering key assets to certain individuals, whose empires were allowed to flourish in return for unconditioned political support. Paradoxically, those who gained control in the lawless environment of 1990s Russia have recently become the most active proponents of the reforms that call for the rule of law (Woodruff, 2004).

#### 1.4 The Role of Legislation in Russia

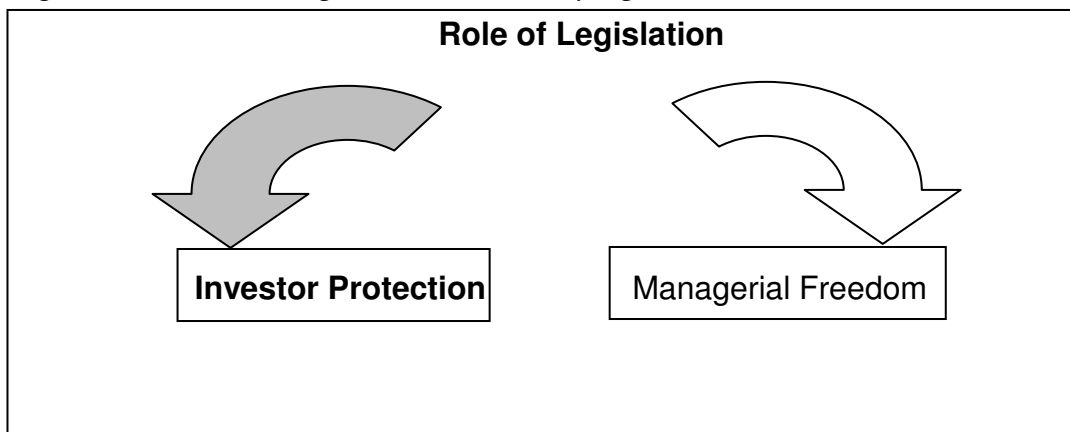
The role of corporate legislation in developing economies such as Russia is fundamentally different from that in developed economies. Here, the primary role of legislation is the protection of investors’ interests from the self-benefiting actions of insiders. The law on joint-stock companies in Russia provides reassurance of the status and position of the company in the eyes of investors (Black *et al.*, 1999). This is a challenging task, particularly with the absence of the essential market institutions and the required social and management traditions and culture. The balance in favour of investor protection inevitably diminishes managerial freedom because it comes in the form of compulsory rules and prescribed practices. It diminishes managerial freedom because the business process is too complex and

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<sup>7</sup> In the context of Russia’s transition from command to market economy, shock therapy refers to a process of rapid privatisation of previously state-owned assets. Although defended by some academics (Shleifer & Triesman, 2005) the practice was severely criticised because, at the time, the country’s institutional infrastructure was completely unprepared to deal with such a drastic change (Black, Kraakman & Tarassova, 2000).

deals with too many uncertainties to be systematically consistent with ‘bright line’ rules which need to be blindly adhered to. However, in the Russian context there is a lot of rationale in sacrificing managerial freedom to act in the interests of shareholder rights. The argument here is that it is that same managerial freedom which is likely to lead to misappropriation of shareholder funds if deliberately misused by insiders (figure 2.2). Furthermore, an ownership structure where majority control typically belongs to insiders and outside shareholders take up the role of the minority makes the governance structure in Russia even more vulnerable to expropriation practices. This ultimately leads to the negative political side-effect of growing public dissatisfaction with the concept of market economy and property rights. This political pressure further emphasises the protective role of prescribed legislation that inevitably curtails managerial freedom.

Figure 2.2: *Role of Legislation in Developing Economies*



### 1.5 Institutional Infrastructure in Russia

In terms of the institutional infrastructure in Russia, Black & Tarassova (2002) have discussed the complexity of the required reforms and their interrelatedness<sup>8</sup>. Ten broad categories that influence the core of the required institutional reform have been proposed in the order of importance: anti-corruption efforts, tax reform, macro-economic policy, small business development, commercial law reform, law enforcement institutions, competition and trade policy, privatisation and

<sup>8</sup> The academics produced a diagram that depicts elements of legal, institutional and microeconomic reform required in Russia. The extent of the complexity of the task of reforming formal institutions is truly incredible with e.g. cultural and religious components being an important addition to the more obvious elements related to anti-corruption and economic reform.

restructuring, banking and land reforms. It has been proposed that during the first three years of Putin's rule some improvement in Russia's business environment has been achieved<sup>9</sup>. More recently, Woodruff, (2004) proposed an account of the institutional context in Russia by examining Russian privatisation and subsequent conflicts over corporate property rights. He proposed that the clarification of the political trajectory will lead to stronger property rights in Russia. Roberts, (2004) discussed the relationship between corporate governance practices of Russian companies and the internationalisation of the financial markets. He identified a general trend towards the Anglo-Saxon model and a notable improvement in the conduct of specific companies when they become exposed to international capital markets.

Generally, this stream of literature concludes that over the past decade, there has been a moderate improvement in the Russian institutional infrastructure and corporate governance in general. However, it is impossible to tell whether the business climate is changing from within or simply looks glossier because of the influx of petrol dollars.

Furthermore, there is a consensus among both academics and practitioners that some important aspects of corporate governance in Russia still lag far behind international standards. It has been previously mentioned that the lack of the rule of law and dysfunctional enforcement mechanisms represent the most important deficiency in Russian corporate environment. Below is a review of the challenges to the rule of law and alternative enforcement strategies that exist in the country.

## **1.6 The Rule of Law in Russia**

In general terms, the rule of law describes a fair and formal process by means of which all aspects of society function. Here, arbitration is based on clear rules, which ideally, everyone is aware of. Enforcement of these rules is carried out by means of formal institutions such as courts which have the power to sanction non-compliers. Moreover, the severity of sanctioning must be strong enough to act as a deterrent for potential violators and non-compliers. In order for a country to have

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<sup>9</sup> Albeit at the expense of one or two oligarchs who had alternative political ambitions.

the rule of law, existence of uncorrupt formal institutions is necessary (Charkham, p.5, 2005).

'The un-rule of law' is a term used in the work of Gel'man (2004) and refers to the dominance of informal institutions and networks which act as a major obstacle to the development of formal institutions and hence the rule of law. In the Russian context, it has been argued, that the dominance of such institutions together with selective application of law and corrupt regulatory bodies present one of the major challenges to the development of corporate governance (Kochetigova *et al.*, 2004).

More specifically, capital markets are directly contingent to the rule of law in that investors' confidence will be high in an environment of homogeneously enforced laws. Confidence in formal institutions translates into a significant reduction in the cost of capital (Mueller, 2006) and stimulates the flow of resources to companies. Moreover, a positive correlation between the rule of law and the size of capital markets has been suggested by a number of prominent studies in the area of corporate governance (La Porta *et al.*, 1997; Modigliani & Perotti 1997; La Porta *et al.*, 1998). In the west, capital markets are relatively developed, in part for the above reason.

Although as far as Russia is concerned, there is no evidence that the size of the financial markets can be affected solely by the improvements of the legal infrastructure (Pistor & Xu, 2005), it is generally agreed that effective regulations are the 'minimum requirement' for the developed capital markets and corporate governance (Roberts, 2004; Pistor & Xu 2002; Pistor & Xu, 2005).

In Russia however, to a large extent, capital markets have been taken out of the equation. The line of causality that has brought about this effect appears unclear. It has been argued that the root cause of underdeveloped capital markets in Russia has been the rent-seeking motives of government officials and other influential stakeholders who prevent the required development of the legal framework (Modigliani & Perotti, 1997). Some suggested that the swift change from state rule to the market model created the legal vacuum that gave rise to massive self-dealing opportunities and discouraged potential investors (Black *et al.*, 2000). Yet others explain this fact in terms of the genuine evolutionary process

inherent to and typical of regime change (Shleifer & Treisman, 2005). Regardless of causality, the fact that there is the 'unrule of law' and underdeveloped capital markets is difficult to challenge in modern day Russia. In broader terms, the phenomenon can be attributed to the lack of the capacity of the state and the legacy of the past (Gel'man, 2004). The latter is a constant feature although with time, its effect is likely to erode as 'new history' and culture is created (Helmke & Levitsky, 2004). The former however, is a more dynamic feature in that it is subject to political forces and the subsequent change in the design and effectiveness of formal institutions<sup>10</sup>.

It has been suggested that the absence of the rule of law leads to the dominance of informal institutions, which in turn prevent the development of legal infrastructures. This is the case in Russia (Gel'man, 2004; Preobragenskaya & McGee, 2004). Informal institutions here are likely to create non-contractual enforcement mechanisms which will allow influential actors to collaborate within closed networks, for example cross holdings and private clubs (Modigliani & Perotti, 1997). These social networks transmit informal rules that fill the gap created by inchoate laws and/or ineffective enforcement. In terms of the latter, informal institutions tend to be characterised by different mechanisms of enforcement in comparison to the formal ones exercised by the police and courts. 'Informal sanctioning mechanisms are often subtle, hidden and even illegal. They may range from hostile remarks, gossip, ostracism, and other displays of social disapproval to extrajudicial violence' (Helmke & Levitsky, 2004, p. 733).

It is critically important to have a deep understanding of the informal rules and associated enforcement mechanisms prior to committing to a contractual relationship with a partner who is conditioned by such an environment. The investigation needs to produce substantial knowledge about the informal arrangements in the Russian business community and the power distribution within it.

The Russian government headed by Putin's administration has achieved some success in regaining the capacity of the state (Gel'man, 2004). This, together with

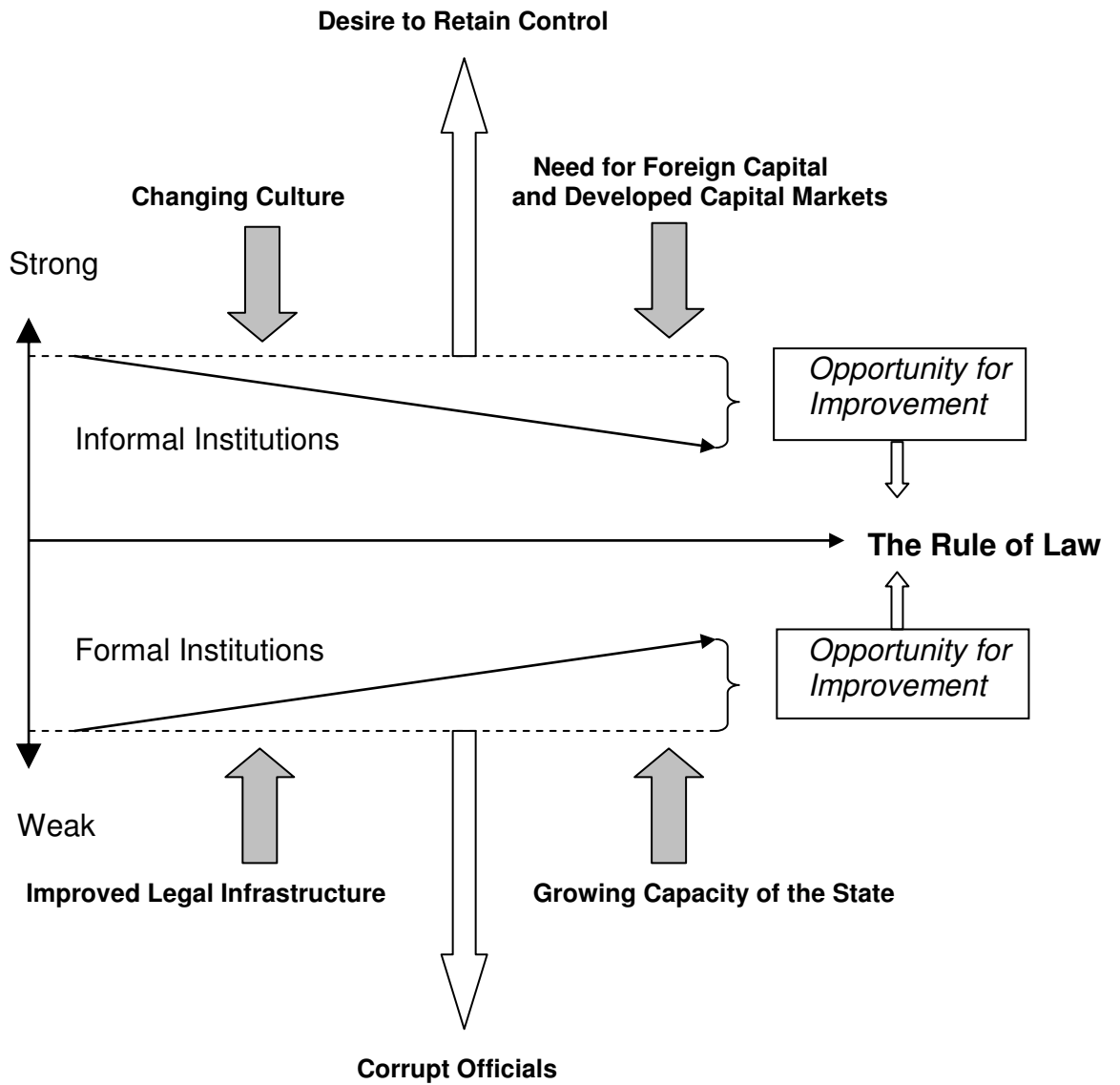
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<sup>10</sup> This dynamic is most visible when a new political clan comes to power. It took less than a year of Putin's presidency for analysts to declare an improvement in the country's business environment.



marginal improvements in the legal infrastructure should lead to a redressed balance in favour of the rule of law (Kuznetsov & Kuznetsova, 2003). This fact, assisted by the change in culture and the need to attract foreign capital should lead to the diminishing relevance of the informal institutions. It is expected that these trends will have a positive influence on the development of capital markets and reduce the importance of the informal networks. However, there are active forces opposed to this change. These forces are represented by the desire to retain power on the part of the informal institutions and by corrupted officials resisting institutional reform. A positive trend in the institutional context is likely to happen where the forces behind establishing the rule of law prevail. This would lead to opportunities for the development of the corporate governance system in Russia and bring it in line with western practice. Conversely, if the forces resisting this change prevail, the negative trend may lead to a threat of deterioration. Hence, it is proposed that opportunity for improvement will be substantiated if corporate governance reforms make formal institutions stronger and informal ones weaker.

Figure 2.3: Dynamics of the Institutional Change in Russia



## 1.7 Research Question Revisited

Any corporate governance system is best tested by its exposure to situations with opposing interests and claims. Hence disputes are chosen as the unit of analysis for this study. The key research question here is whether there is a noticeable change in the composition and type/style of institutional involvement in the process of corporate dispute resolution. By analysing both disputes and methods of their resolution in the Russian environment, the researcher seeks to identify influential parties and assess the nature of their involvement in the process of resolution. Such analysis will facilitate the identification of both positive and negative forces within the environment that explain the changing nature of the institutional infrastructure and corporate governance.

This method of analysing corporate governance is deemed more applicable to less developed countries and transition economies where courts are generally less capable of resolving corporate disputes adequately and stakeholders have to employ a variety of methods to protect their interests<sup>11</sup>.

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<sup>11</sup> Conversely, in countries with a developed legal infrastructure, a dispute is normally identified by a legal action. In other words, in an instance of a conflict, affected parties trust legal arbitration and accept the authority of the courts.

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## Section 2: Corporate Disputes and Enforcement Practices

This section provides a definition of corporate disputes and enforcement practices prevalent in Russia.

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### 2.1 Defining Corporate Disputes

Altogether only two academic studies have been found that provide a comprehensive review of the nature of corporate disputes in Russia. Both studies seek to provide a holistic view of prevailing value-destroying practices which are unique to the Russian context. Moreover, agency theory is featured in both studies and serves as the theoretical prism through which corporate violations are categorised.

The most recent attempt sub-divided corporate violations into disenfranchisement and dilution practices (Dyck *et al.*, 2008). The former category refers to attempts by controlling shareholders to prevent other stakeholders from influencing corporate decisions. Here, the practice ranges from corporate bullying to preventing access to general meetings. The second type of violation refers to various forms of share dilution (closed share issues, unfair share swaps, self-dealing transactions, creditors reallocating assets to themselves via bankruptcy proceedings, flawed appraisals of assets and other less obvious forms of share dilution).

The second categorisation was proposed by Fox & Heller (2000) who developed a framework of Russian corporate governance pathologies. The framework and 'pathologies' set the context and explain the nature of corporate disputes in the country. Here corporate conflicts are also divided into two broad areas: non-maximisation of residuals and non pro-rata distributions (appendix 2). The first broad type of corporate violations refers to a failure to manage corporate entities in a wealth-maximising fashion. Here, managerial incompetence, managerial inaction, lack of authority, and other factors<sup>12</sup> that prevent creation of wealth are mentioned. The second category refers to inadequate compensation for shareholders in proportion to their ownership stake<sup>13</sup>. Failure to distribute claims

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<sup>12</sup> Both internal and external to a firm.

<sup>13</sup> Once wealth has been generated, it needs to be distributed fairly.

constitutes a corporate violation of the second type. This category is further subdivided into diversion of assets when corporate property is squandered and diversion of claims when existing shareholdings are diluted.

Furthermore, the Russian law on Joint Stock Companies (1996) has been reviewed for additional information about potential categories of corporate disputes. Here, the foundation, re-organisation and liquidation of a company, register of shareholders, issue and redemption of shares and other securities, payment of dividends, board of directors, major transactions, self-dealing, control, disclosure and accountability have all been identified as key areas where potential corporate conflicts can occur.

## **2.2 Enforcement Practices**

The low level of law enforcement in Russia has been identified as a central problem that renders the very existence of most governance institutions virtually ineffective (Kochetygova *et al.*, 2004). The mass privatization strategy adopted by the Russian policy makers and encouraged by influential Western advisors has resulted in a questionably just and legitimate ownership transformation process of a large proportion of valuable national assets (Black, *et al.*, 2000; Fox & Heller, 2000; Woodruff, 2004). Miss-allocation of property rights destroyed previously established matters of de facto managerial ownership making it impossible to exert legal control over the process (Woodruff, 2004). Consequent enlargement of the ownership chains made law enforcement impossible in the country where available legal mechanisms did not have enough time to readjust to meet the challenges of the newly established market economy.

As previously stated, those who gained control in the lawless environment of 1990s Russia have recently become the most active proponents of the reforms that call for the rule of law. Initially, these reforms were allegedly blocked by the same individuals at the onset of the transition. The argument here is twofold. Russia is ruled by unscrupulous owners who became rich by misappropriation of the economy at the time when it was most vulnerable and defenceless. They are the individuals responsible for practically every known pathology of corporate

governance (Fox & Heller, 2000). On the other hand however, current owners, having achieved the desired status, developed their understanding of the market economy to the extent necessary to realise that absolute legitimacy is the only way forward if the great potential of capital markets is to be tapped into (Woodruff, 2004). A fundamental shift towards greater legitimacy is an indication of the existence of the motivating factors dictating law-consistent actions. The nature of the latter is not connected with a conscious effort towards legal reforms, but is to a large extent driven by non-legal motives, such as the desire to retain overall existing control over property rights. The non-legal motives are the ones that fall outside the sphere of legal sanctions and therefore do not require external enforcement<sup>14</sup>. The positive trend here is that regardless of the underlying motive that determines the means, the end will invariably be justified by a more effective legal system. The study of the role of law in enterprise transactions contains the proof of the latter, and demonstrates that litigation can be an important and workable enforcement strategy in Russia (Hendley *et al.*, 1999). However, in an environment where formal rules are contradictory and unstable, litigation can also be used as a business filter and barrier working in the interests of a small group of influential actors (Radaev, 2003). The fact that a number of enforcement strategies exist, suggests therefore that litigation is not the absolute determinant of corporate conflict resolutions. These strategies and their importance in relation to enterprise behaviour in Russia are considered hereunder.

### **2.2.1 Relationship-Based Enforcement**

This form of enforcement uses the refusal to cooperate in the future as a main deterrent from breaking an agreement. It is most effective when it is difficult to find an alternative trading partner, investor, resource, etc. on the same economic terms (Johnson *et al.*, 2001).

Small, probing contracts, deals and arrangements play an important role in establishing the initial business contact. Typically, if unfavourable contractual

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<sup>14</sup> In other words there is no need to compel an owner to act as an owner, because it is in his/her self-interest to do so anyway. If self-interest can be better served by adhering to basic rules, than most owners will ensure that this is the case without the necessary legal enforcement.

conditions prevail at this stage, they will serve as a test of trustworthiness and help to acquire the practical experience of working with the chosen partner (Radaev, 2003). These unfavourable conditions will act as an incentive not to break the terms of the agreement once the required level of understanding and acceptance has been achieved. It is important that the latter condition is followed by the subsequent improvement of the arrangement to the mutual benefit of the partners. This benefit comes in the form of both financial gains from the reduced cost of transactions, and the simplification of operating procedures.

Knowledge of the background and specific characteristics of a partner will provide a degree of influence when it comes to the actor's willingness to conform to the terms of the agreement (Johnson *et al.*, 2001). This influence is likely to be in the form of informal sanctions detrimental to the partner's reputation or social standing (Dyer, 1997). Clearly, such sanctions will have a greater leverage in relation to long established partners whose main asset is their reputation. Interestingly, it has been suggested that under such circumstances, litigation is also an effective strategy which paradoxically complements the relationship-based contracting in Russia (Radaev, 2003).

Additionally, and as an indirect function of the above, trust is considered as a mechanism of enforcement, as the existence of such reduces the cost of transactions (Madhok, 2005; Madhok, 2006). Trust will act as an effective leverage of enforcement if preserving 'goodwill trust' translates into greater savings on transactions in comparison with the savings resulting from non-compliance (Dyer, 1997). Russia is a comparatively low trust country, characterised by ineffective formal institutions and frequent infringement of business contracts. It is no surprise that honesty in relations here is hard to achieve, but is generally regarded to be of great value (Radaev, 2003).

It is important to acknowledge at this stage, that in international joint ventures, a degree of asymmetry will inevitably be present in relation to interpretation of the concept of trust (Zaheer & Zaheer, 2006). In Russia relationship contracting is the most significant enforcement strategy (Hendley *et al.*, 1999). This is an important feature which to a large extent determines the required level of cooperation founded on trust. It is likely that the Russian companies will want to see a greater

level of trust facilitating enforcement in international ventures in a conscious effort to preserve confidentiality. It is this same confidentiality that has up until now blocked comprehensive corporate governance studies on the enterprise level (Fox & Heller, 2000).

Relationship-based contracting is characterised by high set-up costs of collecting business data, but mitigated by lower transaction cost over a longer term (Dyer, 1997). The latter consideration suggests that this enforcement strategy is particularly relevant when the parties involved are seeking continual commitment in an environment characterised by a weak legal infrastructure and poor institutional support.

### **2.2.2 Self-Enforcement**

Self-enforcement is a widely used strategy in Russia as it does not require any participation from a third party (Thornton & Mikheeva, 1996). This is an important consideration since in Russia there is little predictability when it comes to dispute resolution by impersonal legal and market institutions. Here, applied mechanisms of enforcement seek to create a mutually beneficial arrangement. It is achieved by voluntarily giving up control over interests in non-enforceable agreements in return for control over interests in agreements where enforcement is possible. If a foreign partner invests in Russian assets which are vulnerable to expropriation, in the absence of prior working experience between the partners, the Russian partner must compensate by having an equivalent financial exposure in the jurisdiction or control of the foreign partner. (Hendley *et al.*, 1999). These sanctions determine the 'self-enforcing range', which is an indication of how robust the contract between the partners needs to be under volatile external conditions (Gow *et al.*, 2000; Gow & Swinnen, 2001). This enforcement strategy is considered an effective strategy when there is little knowledge or influence over the partner's behaviour. Despite the fact of the initial limitation on net investment, this arrangement leads to the build up of trust and reputation once the message of mutual benefit has been understood by the parties involved. Careful investigation of the reputation and track record of a potential partner can be carried out during this initial stage of cooperation characterised by formal self-enforcing



arrangements. Once the required level of confidence has been achieved, formal control can be relaxed, facilitating further investment and reducing transaction costs. This confidence however, has to be supported by economic consideration whereby future opportunities of cooperation must outweigh immediate benefits from non-compliance (Thornton & Mikheeva, 1996).

### 2.2.3 Third-Party Enforcement

Third-party enforcement is gaining momentum in contemporary Russia (Hendley *et al.*, 1999). It can be considered as a strategy which is one step closer to formal and official enforcement. To a certain extent the arbitration and enforcement function here is delegated to a third party. This kind of enforcement prevails over litigation only if business actors have a greater trust in the conflict-resolution assistance coming from a reputable third-party enterprise. This seems to be the case in Russia as businesses tend to view themselves as 'us' versus 'them', the latter meaning authorities (Radaev, 2003). It is for this reason that non-competing companies chose to be more open with each other, rather than the state (Hendley *et al.*, 2000).

Although there have been cases where the intervening third party had no direct interest in such enforcement, what really makes this strategy work is the interdependency of the organisations involved in the dispute (Hendley *et al.*, 2000; Radaev, 2003). Conflict resolution is straightforward under the circumstances where there is a dominating entity capable of exerting control over adjacent companies. The rise of the Financial Industrial Groups (FIGs) in Russia is clearly an indication of the presence of such dominant forces with substantial enforcement capabilities. These industrial groups are fighting for legitimacy and general acceptance by the business community through being the most active proponents of law and order, a difficult and controversial task given the not so distant history of Russian privatization (Woodruff, 2004).

By way of contrast, it has been suggested that FIGs do not play an important role in contract enforcement in Russia (Hendley *et al.*, 1999; Hendley *et al.*, 2000). However, the explanation for this might be the fact that most commonly these

groups are viewed as an absolute authority with extensive governance functions (Brown *et al.*, 2000). It is considered impossible to challenge the latter and hence most companies simply comply even though their interests might not have been fairly represented. This fact is particularly relevant to market entry and competition disputes.

Financial Industrial Groups in Russia are typically closely associated with a friendly bank. This fact makes these groups very effective at enforcement, particularly in relation to independent companies using the services of such a bank. However, since the Financial Industrial Groups in Russia have substantial economic powers, they have a propensity to use those powers in their own interests, thereby benefiting affiliates and disadvantaging independent entities (Kochetygova *et al.*, 2004). This fact constitutes a degree of asymmetry in the actual enforcement role of the industrial groups in Russia.

In the absence of a dominant player, third-party enforcement is carried out through business networks and associations (Hendley *et al.*, 2000). Breaking the rules of such institutions may result in a non-performing company being added to a blacklist. This form of enforcement is effective when there are tangible benefits to be gained from being a member of such organisations. Business associations are at the evolving stage and are likely to gain relevance in Russia as the advantages from membership become more evident.

Finally, as the capital markets develop further, auditors, debt rating agencies, security analysts, and other parties involved in floatation procedures gain importance and act as facilitators of the culture of formal compliance and enforcement (La Porta *et al.*, 1998). This fact arises from the potential of a greater financial benefit when seeking floatation as available capital resources are on the increase.

#### **2.2.4 Private Enforcement**

Weak legal infrastructure has been a characteristic of post-Soviet Russia (Thornton & Mikheeva, 1996; Hay & Shleifer, 1998; Kochetygova *et al.*, 2004). The state legal system is not used because it provides an inefficient and overly

expensive service. Moreover, businesses are unwilling to expose themselves fully to the authorities because as a rule their legitimacy could be called into question. Unsure of the officials' reaction to the inherent discrepancies in business conduct, companies are cautious about using the legal system in case it should turn against them (Hay *et al.*, 1996; Hay & Shleifer, 1998).

Private enforcement is believed to have taken an active role in filling the legal vacuum (Hay *et al.*, 1996; Hendley *et al.*, 2000). It has done so in two forms: private arbitration tribunals (Treteiskie courts) which are recognized by the existing legal system and private security firms which are generally perceived as less legitimate (Hendley *et al.*, 2000).

When using private arbitration tribunals disputants need to acquaint themselves with the varying procedural rules. This consideration, to a certain degree, limits the number of such tribunals that can be used simultaneously. This is specifically the case in Russia where Treteiskie courts typically specialize in a very narrow area of dispute resolution. Normally, parties to a contract would choose a 'friendly tribunal' which is not necessarily completely biased, but is expected to protect the interests of the nominating party. On the other hand, the reputation of such tribunals is their most valuable asset since they exist on the fees paid by the companies. Such exposure to the market forces will compel the tribunals to provide the services which are required by the market participants. They will supply fair arbitration if the demand dictates so.

As far as international cooperation is concerned, the likelihood of a Russian arbitrator being nominated is very low. The Stockholm or London courts are the much preferred option of the foreign partners where local legislation permits (Hay & Shleifer, 1998).

Private security firms are considered for use when there is no pre-existing relationship between parties to a contract (Hendley *et al.*, 2000). Their main advantage is the speed of enforcement. Private security firms are not concerned with looking for a fair dispute resolution, but simply represent the interests of the party that offers more money. Hence, their enforcement is not characterised by a great deal of procedural consistency, but may be chosen for its responsiveness. Frustrated with endless bureaucratic hurdles intrinsic in the official process,

companies may opt for the methods which represent the alternative extreme of the enforcement continuum, falling outside the legal zone. Interestingly, but not surprisingly, a lot of organisations fall into the trap of choosing this method of enforcement. It is a trap, because a great many companies in Russia operate in an extra-legal environment (Hay *et al.*, 1996). Once exposed to a private security firm, companies find it almost impossible to disassociate themselves from the former. Private enforcement firms may and do use their knowledge of the extra-legal activities of a firm as a form of coercion in order to guarantee continuing cooperation.

Generally, there is consensus among academics that private security firms' enforcement is inefficient in the new Russia (Thornton & Mikheeva, 1996; Hay & Shleifer, 1998; Hendley *et al.*, 1999; Hendley *et al.*, 2000; Yakushin, 2003; Woodruff, 2004). This type of enforcement, although speedy and powerful, is also described as incompetent, unstable, uncertain, costly and lacking confidentiality. Further study has found evidence of very limited use and importance of this type of enforcement in Russia (Hendley *et al.*, 1999). However, it has also been suggested that it is impossible to eliminate private security firms from today's Russia because they have too big a role in protecting property and money (Hay & Shleifer, 1998). Hence, every effort should be made and is being made to readjust their practices to ones which are socially acceptable, a move which will lead to a possibility of future legal acknowledgement. This can be done by clearly separating the arbitration and enforcement functions. Here, arbitration should be carried out by more competent private arbitration tribunals and then enforced by means of private security firms. Bright line rules are the essential facilitators of the arbitration stage (Hay *et al.*, 1996), while the existing social norms would dictate acceptable enforcement practices. This arguably more balanced allocation of enforcement responsibilities is expected to lead to a greater convergence of the dispute resolution mechanisms applied in Russia. Unfortunately, as a result of mass exposure to state oppression, Russian society has developed a great deal of tolerance towards violent enforcement. It is this passive complacency, a legacy of brutal state control that lends itself to the acceptance of violent enforcement in the business community (Levin & Satarov, 2000). However, with the new regime, the

social norms should rapidly evolve until eventually, violent measures become prohibitive.

### **2.2.5 Administrative Levers of the State**

Government officials have significant influence and effective enforcement mechanisms at their disposal in relation to their involvement in dispute resolution. These mechanisms come primarily in the form of the officials' ability to assist or impede a company's efforts to ensure compliance, specifically along the bureaucratic dimension (Roaf, 2000). Moreover, officials have substantial arbitrary and discretionary powers as the legal system lags behind the country's market reforms (Roaf, 2000; Kochetygova *et al.*, 2004). Therefore, affiliation with local authorities is regarded as a practical measure which facilitates the enforcement capabilities of an enterprise (Levin & Satarov, 2000). At the federal level, all major companies are careful about not upsetting the state since the latter is capable of selective action. The fact that in the 1990s it was almost impossible to conduct business in Russia absolutely legally, gives the state necessary leverage and control over influential enterprises. The trade-off here is an informal agreement between the officials and businessmen where the former agrees not to press for tax and other allegations so long as the latter supports and accepts the authority of the state. At its worst, this interaction may fall into the category of high-level corruption where the terms are dictated by a political and business elite (Roaf, 2000). This situation is difficult to rectify because the interests of very influential parties are at stake. However, current administration makes systematic efforts to redress the balance by means of administrative reforms which seek to reduce the role of government, simplify procedures, improve the rulemaking process, and increase transparency (Black & Tarassova, 2002). All the above mentioned measures seek to reduce the levels of corruption among Russian officials at both local and federal levels.

Currently, available administrative levers are used for two purposes and with completely different objectives with regards to contemporary businesses.

The first broad application is connected to the ongoing power struggle between the current government, and influential business parties in relation to political issues and ownership of strategic assets. Here, the former does not hesitate to use all the available administrative levers at its disposal. Withdrawal of licences, privileges, and approvals, ownership and tax claims, denial of access to valuable resources, privatization allegations and endless bureaucratic measures are applied on an arbitrary basis and are used to coerce non-conforming organisations (Levin & Satarov, 2000). Under such circumstances the efforts of the state can be highly organised, systematic and extremely effective.

The second broad application of administrative levers in Russia is a decentralized and extremely ad hoc phenomenon whereby underpaid officials seek to exploit their position of power for personal gain (Levin & Satarov, 2000). Rules and regulations that encourage bribery and corruption, lead in themselves to a demand for the creation of more official posts, further expanding a self-perpetuating administrative sector. The latter has then to come up with more rules and regulations so that more bribes can be collected. At one time, the whole of the Russian economy was infected by this characteristic (Black *et al.*, 2000; Levin & Satarov, 2000; Roaf, 2000). The ongoing administrative reform is primarily directed at tackling this particular misuse of the administrative levers.

### **2.2.6 Shadow of Enforcement**

Threats of enforcement act as an enforcement strategy in their own right. There are two directions a company can pursue within this category of enforcement in Russia. The first direction is also applicable to more developed countries and is frequently referred to as the shadow of the law (Hendley *et al.*, 1999). Threats to pursue legal actions act as a robust enough deterrent from breaking the terms of a contract, particularly if the latter includes collateral or penalty clauses. It is different from self-enforcement in that here, although as a last resort, the parties still do rely on taking the case to court. Under these circumstances, the actors involved in the conflict accept the authority of the court and its enforcement capabilities. However, ultimately a non-conforming business partner might choose to comply and not use the services of the legal system because of the associated high legal costs and

the potential imposition of sanctions. The threat of legal action is an effective enforcement strategy in Russia where penalty clauses and official letters of complaint often provide room for further negotiation rather than initiate legal action (Hendley *et al.*, 2000).

The second direction involves the threat of private enforcement and is generally regarded as more specific to Russian circumstances. This strategy is applicable in situations when the characteristics of a partnership are such that legal action is impossible or ineffective. If the parties to a contract recognize that their interactions fall outside the legal enforcement range, they will turn to private security firms (Hay & Shleifer, 1998; Black & Tarassova, 2002). As discussed earlier, such firms are expensive to use and once employed, they are impossible to disassociate from. However, because private enforcement is responsive and powerful, it is feared by most market participants and therefore the potential use of such methods sends a strong signal to the non-complying party. Here, companies tend to disclose which private enforcement agency they have access to at the initial stage of cooperation and in most cases this will be sufficient to ensure compliance within the terms of the agreement. In practice there has been a fairly low instance of resorting to the actions taken by the actual agency (Hendley *et al.*, 1999). This is indicative of the fact that this strategy does not require aggressive actions, as parties will look for a mutually acceptable solution with the fear of private enforcement serving almost as a motivating factor. According to some academics, this enforcement capability creates a unique business environment in Russia which reinforces control over parties with potentially conflicting interests and helps to maintain the status quo.

### **2.2.7 Litigation**

The most prominent safeguard against non-compliance employed in the West is the legal contract (Dyer, 1997). This type of enforcement requires a high level of formality in the interactions which are supported by the power of institutions in an environment of maximum transparency (Roaf, 2000). In Russia however, the effectiveness of this enforcement strategy has been questioned. It has been argued that corrupt officials right across the institutional infrastructure render this

enforcement strategy unusable for legitimate organisations (Levin & Satarov, 2000). Contradictory and incomplete laws coupled with incompetent and inexperienced judges result in an unacceptably low level of predictability within the legal system. Finally, this system has no effective means of enforcing its decisions once a ruling has been made (Hay & Shleifer, 1998).

Conversely, it has been suggested that a marginal improvement has been achieved through the ongoing legal reform (Black & Tarassova, 2002). Some critical elements of the legal system are being addressed and in doing so important legal loopholes are being closed. This encourages the use of litigation as a plausible enforcement strategy in Russia (Hendley *et al.*, 1999). By addressing critical issues associated with the tax system, commercial law, legal aspects of enforcement institutions, competition and trade policies, banking reform, market reform, and land reform the central government is making a systematic attempt to re-establish law and order in the country. Proposed laws are set to accommodate current business practices better and seek to work with rather than against already established organisations. Arbitrary dimension of the legal system is diminishing. Bright-line laws are being introduced and contradictory laws eradicated. As a result, the bureaucratic system is becoming less prone to corruption and more efficient at performing its functions. However, 'cleaning up' the legal system is recognized to be a lengthy process and the current situation, although positively influenced by the emerging free market infrastructure, still requires a great deal of anti-corruption measures.

Therefore, the logical question to ask is how litigation, as a dominant enforcement strategy in the West, changes and evolves in an environment where the relationship-based approach prevails. In order to gain a greater insight, the practical strategies of enforcement adopted by the cooperating parties need to be analysed. It is unlikely that there will be a single strategy chosen, but rather an amalgamation of the most effective ones under the circumstances. The emphasis attached to a particular approach will be an accurate indication of the prevailing/dominant system.



### 2.3 Research Question Revisited

On a national scale, the development of greater investor protection, increased market control, shift towards the rule of adequate laws and more sophisticated judiciary are all complex processes which individually and as a whole are not subject to a single reform. The complexity arises from a great variety of both dynamic and inert factors at work. Looking for a relationship between a specific development and the trend in institutional dynamics will not produce meaningful results for that very reason.

In order to identify the trend in institutional development the following tasks are proposed:

1. Identify conflicts and methods of their resolution at the beginning of transition
2. Identify key institutions involved in the process
3. Identify conflicts and methods of their resolution in the modern environment
4. Identify key institutions involved in the process
5. Analyse the degree of influence of each institution.

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## Section 3: Media

This section considers the role of media with reference to the study. It also provides a revision of the research question.

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### 3.1 The Role of the Media in the Study of Russian Corporate Governance

Another literature stream that this study relies on seeks to formulate the role of the media in corporate dispute resolution. In discussing some of the key works in this area, the role of corporate governance in the context of agency theory will be highlighted.

Despite the frequently acknowledged impact of media on the development of corporate governance, there have been few attempts at formulating this influence in terms of academic theories and frameworks. Arnold *et al.* (2007) call for more research into the connection between media coverage and corporate governance. Their research looked at the share price performance of companies further to their appearance on the front page of a popular business publication. This positivistic study concluded that extreme performance (good or bad) comes to an end when a company appears in a front page report. Earlier, Pollock & Rindova, (2003) refer to press as 'expert monitor' which role is to facilitate the exchange between buyers and sellers, but also highlight the role of media in forming perceptions about appropriateness of firm actions. The former role of media has led academics to conclude that publishing unreliable information would result in readers making unprofitable investments, forcing them to turn to alternative sources of information (Johnson *et al.*, 2005). Hence, there is incentive for newspapers to represent reality accurately if copies are to be sold in good numbers. The same academics concluded that vigilant press will act as a corporate governance mechanism and prevent managerial expropriation by investigating and reporting on corporate matters. In this context, financial press not only provides the mirror of corporate environment<sup>15</sup>, but also exerts influence over the decision making process within the system of governance. The latter function of media is further discussed by McCombs (1992) in relation to agenda setting power of media. Skeel (2000)

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<sup>15</sup> Deephouse (2000) emphasises professional norms that would require journalists to produce a thorough record of important events.

considers the role of shaming in corporate law, reinforcing the connection between media and corporate governance through reputational costs. In general, there is a great deal of agreement that media coverage of corporate matters is crucial for the understanding of the development of the corporate governance discipline (Brickey, 2008).

All this said there has been little research into country specific circumstances that play a role in the aforementioned relationship. However, academic literature reveals a number of important factors that need to be considered in the context of studies that seek to investigate corporate governance through the prism of country specific media characteristics.

Djankov et al. (2001) consider patterns of media ownership. Their conclusions suggest that government ownership is generally associated with, among other things, inferior governance. They also suggest that 'the adverse effects of government ownership on political and economic freedom are stronger for newspapers than for television' (Djankov et al., 2001, p 2). Significant state ownership tends to be the case in countries like Ukraine, Indonesia, Saudi Arabia, and Kazakhstan. In the instance of Russia, in the late 1990s, there was a close connection between those who owned the media and the government. This fact allowed the latter to be in full control over information dispersion in the country. With time, ownership of key media outlets in Russia was transferred from 'friendly individuals' to the state. This fact, in principle, further curtailed the role of financial press as an independent governance watchdog. Clearly this development, not only prevents media from acting as a 'mirror' of actual events, but also sets a particular agenda, and hence diverts attention from real governance issues to the ones which are politically 'manufactured'. However, Dyck et al. (2002) argue that in these circumstances, foreign media, if not banned, should fulfil the required role by not being subject to the same intensity of political pressure and influence as local press. Their later research concludes that Russian companies/stakeholders are more likely to reverse their damaging actions if the respective corporate governance violations are reported in western press as opposed to Russian

media<sup>16</sup>. The researchers did not consider the relationship in the context of other countries. There is an inclination however to suggest that former Soviet states would exhibit similar biases against indigenous sources of media and by virtue of that fact would tend to treat western sources of information as more credible. Nevertheless, the same researchers outlined the role of generally acceptable norms of behaviour in a society as a determinant of the impact media is likely to generate on a particular sphere of activity. Here, it is proposed to consider the Russian case as an example of the latter tentative conclusion. If western media reports a severe case of corporate violation, the full impact of media will be achieved only if the investment community interprets the violation as severe. In the Russian context there inevitably will be a degree of asymmetry in this respect. In the late 1990s, internal pricing seemed to be treated as a norm and press reports to that effect did not trouble the investment community (including foreign investors) which was very much used to the practice in question. However, in the context of a more developed country in terms of the corporate governance infrastructure, the same story about transfer pricing would have been interpreted as a severe violation. In the second scenario, the call for the redress of the violation would be much stronger whereas in the Russian example, the social norms would dampen the effect of the report on the subsequent action. The threshold of tolerance is different in different countries and for that reason it is difficult to make any cross country comparisons. However, social norms are regarded as a fairly inert characteristic unlikely to change drastically in a short to medium term. This makes comparison within a particular cultural setting more meaningful.

### 3.1.1 Information Diffusion

In general terms, the role of the media is to present information in a particular way. As far as economic agents are concerned, the immediate benefit here is the dramatic reduction of costs associated with being informed (Dyck *at el.*, 2008). The financial press publishes a lot of information about specific companies and stock markets in general, which otherwise would have been difficult to accumulate.

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<sup>16</sup> The gathered data suggests that in almost 60% of cases redress of violations occurs if disputes are reported in western media.

In many instances had it not been for the press, a lot of investors (and other stakeholders) would not have been informed about their investments/companies to the same extent as they are. This point is supported by the concept of rational ignorance described by Downs (1957) where the cost of not being informed is exceeded by the cost of acquiring information.

Clearly, the press can package information in a particular way (Becker & Murphy, 1993) which means that the information is inevitably presented with an element of bias. The bias can be determined by a variety of factors such as advertising pressures (Reuter & Zitzewitz, 2006), media ownership (Besley & Pratt, 2006), target audiences (Mullinaithan & Shleifer, 2005), and the trade-off between reporters and sources (Dyck & Zingales, 2004). However, in the Russian context political pressures have also been suspected as a source of potential bias (Dyck *et.al*, 2008), particularly in terms of serious concerns over freedom of press<sup>17</sup> (Osipovich, 2008). However, the same authors acknowledged the fact that in Russia, the English language press is unlikely to be subject to the same level of political bias as their Russian counterparts.

Studies which rely on reported material as their source of data need to be mindful of the fact that published material can be strongly influenced by factors that prevent an accurate representation of events. Regardless of the accuracy of representation however, some authors in this stream of literature suggest that the economic impact of media pressure is large (Dyck *et al.*, 2008). This is particularly true with regard to topical issues like corporate governance. Additionally, in perceived terms not only does reported material constitute a significant proportion of such pressure, it also plays an important role in forming opinion and informing actions.

### **3.1.2 Agency Theory and Corporate Governance**

As previously stated, agency theory is the theoretical underpinning of this work. In terms of reported material, the connection becomes evident when reputational

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<sup>17</sup> According to the U.S.-based democracy watchdog Freedom House Russia has the same level of press freedom as Sudan.

costs of negative coverage are considered (Fama, 1980). In theory, managers (and other stakeholders) will be deterred from self-centred actions if the derived benefits are less than the negative impact of punishment and reputational costs (Dyck *et al.*, 2008). The following equation proposes a condition under which self-centred managers will be deterred from violating rights of shareholders/stakeholders:

$$\text{Private benefit} < \text{Reputational cost} + \text{Punishment}$$

In countries where formal institutions are weak, appropriate punishment becomes less likely. This is because courts can be bribed and punitive rulings can be simply ignored. The same applies to other formal institutions that in such environments typically lack enforcement powers. Conversely, in this context, reputation becomes an important asset (Radaev, 2003) and hence reputational damage begins to have a more direct and substantive impact on the decisions of agents whether to engage in value reducing practices or not.

In Russia formal institutions are weak. Often, before committing to a major investment, foreign companies are keen to invite influential Russian counterparts that would assume the tasks normally performed by formal institutions<sup>18</sup>. Often because of the importance of such Russian insiders, foreign companies are prepared to remunerate these individuals very generously. This means that any negative piece of publicity would considerably reduce the chances of such an individual being selected. Hence, the reputational cost of negative publicity in certain instances would act as a strong deterrent from acting in self-interest. The government and state officials would also be subject to reputational costs, but more in connection with electorates' opinion, rather than commercial partners and major shareholders. However, with the increasing role of the state in the business affairs of the country (Gel'man, 2004), investment communities will be on constant alert for any information that would reveal clues about the state's reputation as a key decision-maker in the environment.

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<sup>18</sup> In the Russian context rating agencies like Standard and Poors often refer to the partner risk as opposed to the country risk.

### 3.1.3 Media Effectiveness

The press, as a source of the media, is in an ideal position to inflict reputational costs on various agents. By publishing compromising materials, the value of an individual's reputation can be considerably reduced. At the same time, reputable newspapers base their reporting on reliable facts (or are perceived as doing so) (Dyck *et al.*, 2008). Therefore, influential business people will have an incentive not to generate facts or rumours that would cause a detrimental impact on their reputation. In this respect, media coverage sends a very important message to the business community about the state of development of corporate governance in a particular country. If blatant violations are continuously reported then in perceived terms there is evidence that:

1. Institutions continue to be weak (low risk of external punishment);
2. Self-centred stakeholders derive a greater benefit from expropriation than from being a reputable partner (insignificant reputational costs).

Conversely, if there is a noticeable improvement with reference to the way corporate disputes are reported, then, in the absence of media bias:

1. Institutions become more powerful (a greater risk of external punishment)
2. Key stakeholders derive a greater benefit from good reputation than from immediate gain of expropriation (significant reputational costs).

Hence, media coverage of corporate disputes is an important barometer of corporate governance both in terms of institutional infrastructure and in relation to the individual behaviour of key stakeholders.

### 3.2 Research Question Revisited

This study relies on evidence of media impact (publications in English language press) on corporate governance in Russia (Dyck *et al.*, 2008). Therefore, the boundaries of this research question cannot not be extended beyond the level of perceived change by foreign investors. However, such reliance on media material offers an opportunity to conduct a more holistic investigation into the institutional construct in the country. Here, it is necessary to compare reported material on corporate conflicts because such analysis reveals the sanctioning powers of institutions at work and suggest inferences about reputational costs with reference to key stakeholders. In this respect, the research question has to reflect the evolving nature of the reported material on corporate disputes in the country.

### Outlining the Gap in Literature

#### The Study of Corporate Governance

According to Iwasaki (2007) in order to understand the subject of corporate governance better, it is necessary to examine the discipline from a multi-faceted perspective. In the Russian context a great deal of empirical research has been conducted investigating the relationship between ownership structure and corporate restructuring. However, dominance of this line of enquiry has led to a vacuum in understanding the complexity of factors that determine enterprise behaviour. This study seeks to provide a contribution to the body of literature by analysing corporate behaviour in the context of reported corporate disputes.

#### Development of Formal Institutions in the Russian Context

Second, there is no agreement in contemporary literature on whether formal institutions in Russia are beginning to perform the required role of policing market relations. Some believe that moderate improvements have occurred (Roberts, 2004), while others emphasise the destructive impact of corrupt courts (Kochetygova *et al.*, 2004). Therefore, any additional information about the role of



corporate governance institutions in the Russian context would contribute to the ongoing debate about the trajectory of the development.

### Corporate Disputes and Resolution Methods

Previously, academic studies attempted to classify corporate disputes (Fox & Heller, 2000; Dyck *et al.*, 2008) and methods of their resolution (Hendley *et al.*, 2000). However, those were separate and unrelated classifications. No previous study attempted to look at the evolving nature of both characteristics in conjunction as a tool for the evaluation of corporate governance. This method of analysing the discipline is of particular relevance to countries where a number of enforcement strategies exist (in addition to litigation). Hence, this study offers a greater scope for analysing more intricate details of the development of corporate governance particularly focusing on agency based conflicts when the system of governance is exposed to opposing interests and claims of various stakeholders. Moreover, because of the added dimension, this study is well positioned to complement and contextualise dispute and enforcement related frameworks in the setting of a holistic investigation of corporate governance.

Additionally, looking at the dispute and enforcement frameworks together offers a wide range of applicability and relevance to other corporate governance related research. Here, positivistic studies of the discipline may benefit from an opportunity to identify new variables and further discuss existing ones in the context of a more encompassing set of parameters. Likewise, studies considering 'softer' aspects of corporate governance like culture and attitudes may adopt a similar approach of combining existing frameworks as way of capturing a higher level of complexity of the subject matter.

### The Role of Media in the Study of Corporate Governance

Finally, this research highlights the role of the media in corporate governance studies. Literature on this topic has been extremely scarce and can be taken forward by the study that relies on the proposition that reported material on

corporate violations can serve as a foundation for inferences about the expected development of the discipline of corporate governance (Dyck *et al.*, 2008).

### Chapter Summary

This chapter has presented three sections of literature that have informed and influenced the design of the study. Agency theory has been selected as a theoretical underpinning of this work with reference to the discipline of corporate governance, institutional infrastructure and the role of the media in the Russian setting. Concordantly, the research questions and gaps in relevant literature have been identified and explained.

## CHAPTER 3: METHODOLOGY

### Introduction

This chapter consists of three sections. Section 1 discusses the main philosophical underpinning of this work. The philosophy of pragmatism is introduced on the ontological level with reference to more specific methodological implications for the research design and quality issues. It is argued that pragmatism is an adequate philosophical perspective for contemporary investigations of Russian corporate governance because of the inherently high level of flexibility. The section is concluded with the discussion of the status of the findings in the context of the proposed investigation. Section 2 presents the method of data collection which is based on the archival material of the Moscow Times and a number of semi-structured interviews. Here, the definition of corporate disputes is reiterated in the context of the chosen unit of analysis. The final section explains how the selected method of analysis is applied to the collected data in the context of the main research question. The innovative use of template analysis is explained through a detailed demonstration of the coding process in relation to the reported material selected for the study. Additionally, a clarification of how the interviewed data triangulates the coded material is provided. This chapter is concluded with an outline of the expected original contribution and methodological limitations of the study.

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## Section 1: Philosophical Underpinning

This section discusses the main philosophical underpinning of the study. Pragmatism is considered in the context of the main research question with reference to methodological and research quality implications.

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### 1.1 Research Philosophy

Research philosophy is an interpretative aid that enhances the meaningfulness of scientific findings. A clear benefit of discussing a researcher's view on ontology and epistemology is that it provides an overall context within which a piece of research has been carried out. This philosophical context, unlike subject-based context, is provided by researchers. It is for this reason that within a single discipline, one can find studies adopting a whole range of philosophical underpinnings. The latter point is of particular relevance to social sciences research where there has been a greater degree of tolerance toward 'non-mainstream' methodological solutions. The overall acceptance of these, at times, obscure methodologies probably comes from the non-scientific nature of some of the proposed enquiries. This however, does not necessarily detract from the importance of these enquiries which is a separate and more subject-specific argument. In a number of instances however, lack of such flexibility might lead to a restraint being imposed on a potentially useful investigation.

This research is underpinned by the philosophical stance of pragmatism. Before discussing this philosophical paradigm, it is important to outline the top-down methodological hierarchy that most social sciences and business and management researchers are comfortable with. This outline will provide a point of reference and hence set the scene for a more meaningful discussion on pragmatism.

### 1.2 Top-Down Approach

Some researchers argue that ontology should be at the very top of the methodological hierarchy (Crotty, 2003). Considerations of an ontological nature reveal the much-debated relationship between the truth that researchers are seeking to uncover and reality. Once this relationship has been determined, the

choice of methodology is a matter of adherence to the overriding philosophical principles. These principles determine distinct paths that researchers subscribe to at the very onset of their investigations. A researcher who believes in truth being a single objective reality naturally falls into the theoretical perspective of positivism. Positivism prescribes a quantitative methodology that in turn determines the choice of statistically coherent methods. Conversely, a researcher who is of an ontological view that multiple realities exist sets out on a research journey having a licence to determine his/her own unique truth. Interpretivism is a research philosophy that sits comfortably within such a subjective view of the world. It prescribes qualitative methodology and advocates non-statistical methods which do not seek to correlate or extrapolate, but strive to capture and explain individual scenarios from the perspective of a researcher.

Traditionally, positivism was seen as the dominant view of the world in relation to scientific enquiries. More recently however, interpretivism has found its way and established itself as a valid theoretical underpinning in social sciences research. However, a major criticism of the top-down approach has been the fact that researchers are inevitably faced with substantial constraints and limitations if they choose to subscribe to the subjective/objective epistemological divide described above. Pragmatism addresses this limitation by proposing a new dimension to the philosophical debate about the relationship between truth and reality.

### **1.3 Philosophy of Pragmatism**

Pragmatism has been dubbed an anti-philosophy because it rejects the notion that we should be concerned about what reality is. It does not necessarily reject the philosophical argument altogether, but rather categorically refuses to engage in the debate about the relationship between reality and truth. The justification for such a dismissal is our inability to know what reality is (Rorty, 1982) and hence the efforts of simply representing it accurately are meaningless. Instead, we must strive to construct useful interpretations of surrounding phenomena.

As far as pragmatists are concerned there are two opposing scenarios that we need to consider. The first scenario is a hypothetical one in which a reasonably

accurate representation of reality is proposed as the ultimate aim of the scientific enquiry. However, from the viewpoint of any pragmatist, this scenario is certain to fail at the very onset since, without knowledge of what reality actually entails, accuracy of representation cannot be adequately determined. Nevertheless, this scenario serves the purpose of demonstrating precisely what pragmatists reject.

The second scenario emphasises the inevitable discrepancy between reality and its representation. It proposes that in the context of a scientific enquiry, the accuracy of representation is subordinate to the usefulness of representation (Gibson, 1979). Hence, pragmatism accepts the idea of an inaccurate, but useful representation of reality. Taking this school of thought further, Rorty (1982) excludes accuracy of representation from the philosophical equation with the non-representationalist view where he invites scientists to cope with the world and not seek to represent it. James (1907), in a strongly worded statement, suggests that a large number of philosophical arguments simply fail when they become exposed to the test of reaching a practical consequence. In this regard, pragmatists propose to focus on the creation of knowledge with practicality being the essential criterion for judging meaningfulness (Goldkuhl, 2004).

It is clear from the above that when it comes to the development of research questions, pragmatists need to fulfil the usefulness requirement. This is where an overlap with other research philosophies may occur. It is entirely possible that taking for example a positivistic path may lead to findings with the most practical significance. In this context, pragmatists do not hesitate to imitate positivists or any other research philosophy for that matter. The fundamental difference is that the parameters of research design are not determined on an ontological level, but are the result of considerations of a practical nature. The following quotation from Morgan (1998, p.19) perfectly illustrates the above point:

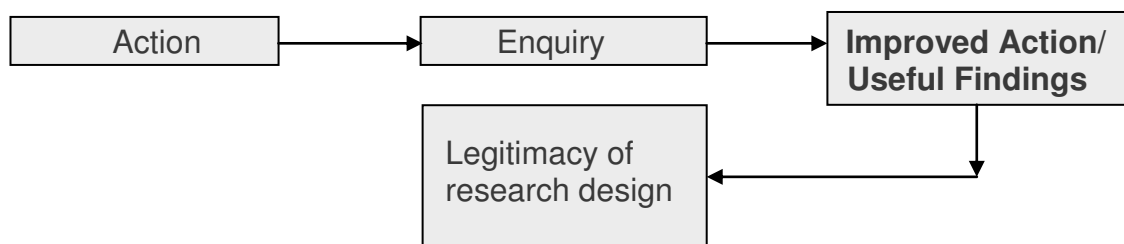
*“Just as we select a tennis racquet rather than a golf club to play tennis because we have a prior conception as to what the game of tennis involves, so too in relation to the process of social research; we select or favour particular kinds of methodology because we have implicit or explicit conceptions as to what we are trying to do in our research.”*

In the context of the above quotation, the question of ‘what we are trying to do’ is unequivocally addressed by pragmatists. They believe that it is the task of

changing our environment in favourable ways (Goldkuhl, 2004) that provides the rationale for scientific investigations. An impact of practical knowledge is considered to be the driving force of the research process.

Following on from the above, a pragmatic piece of research has to identify a concrete action that it seeks to improve. This action is subjected to an investigation which examines/evaluates input from various stakeholders and proposes modifications. The 'new action' is expected to be an improvement on the 'old action' from the perspective of an identified group of stakeholders. Consequently, the level of improvement serves as the criterion for judging the legitimacy of the enquiry. Figure 3.1 is the graphical representation of the latter point. Clearly, at the time of the enquiry itself it is difficult to know whether it would lead to an improved action or not. Pragmatism does not necessarily suggest that enquires that fail to produce an improved action lack legitimacy. But it clearly states that the requirement of usefulness must be fulfilled. This resonates with Goldkuhl (2004) who claims that pragmatism gets its legitimacy from being a servant to practice.

Figure 3.1: *Legitimacy of Pragmatic Research*



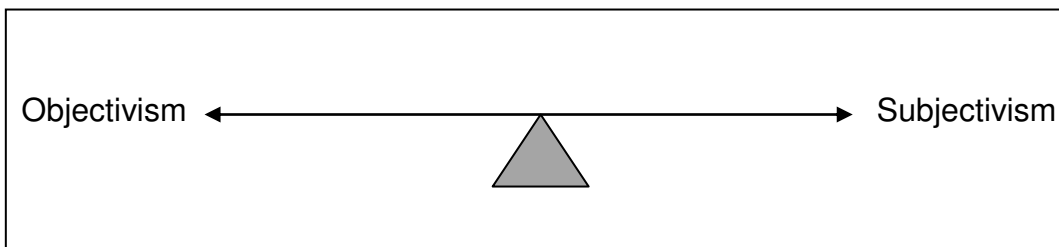
In this regard, pragmatism has a lot to offer social sciences and particularly business and management research where more emphasis should be put on the practical consequences of knowledge (Goldkuhl, 2004).

#### 1.4 Methodological Implications of Pragmatism

Pragmatism does not reject either objective or subjective methodologies. In fact, it refuses to favour one or the other. It suggests that if there is a practical rationale,

the unrestricted choice of methodology is the essential freedom that researchers must have. Pragmatism does not view objectivism and subjectivism as unrelated dimensions, but rather regards them as the opposite ends of the methodological continuum (figure 3.2). The position on the methodological continuum is not so much determined by the researcher's view of the world (ontological level), but is driven by the nature of the research question and practicalities of the research design. As a direct consequence of this, pragmatists have the option to change the degree of objectivism/subjectivism as deemed appropriate in the context of the research question.

Figure 3.2: *Methodological Continuum*



This position has been criticised profusely by both extreme positivists and social constructionists. They are uncomfortable with pragmatism and see it as 'sitting on the fence'. The refusal of pragmatists to identify themselves in objective/subjective terms simply renders their arguments illegitimate. Indeed, one can see the source of confusion and even irritation when pragmatists start changing their world view like gloves, while others are stuck with a single methodology. To 'others' pragmatists are unidentifiable and therefore their findings cannot be viewed within a meaningful/rigorous philosophical and methodological context.

Pragmatists do not reject this criticism outright for they recognise rigour as an important aspect of research. Indeed, if a research design leans towards the subjective end of the continuum, due consideration must be given to the origins and impact of the researcher's bias. Moreover, findings need to be discussed and applied within the boundaries of limited validity and generalisability. It appears that interpretivists would go about the task in much the same way. In this case, the 'sitting on the fence' criticism does not amount to the quality of the findings, but



simply manifests itself in the general unwillingness of pragmatists to commit to a particular methodology. It is understood how this could lead to a certain degree of confusion if not addressed adequately. However, in a true pragmatic fashion, it is believed that if the much criticised flexibility produces tangible benefits where positivists and interpretivists stand a higher chance of failure, the argument of the latter simply does not hold.

### **1.5 Pragmatism in the Study of Corporate Governance**

Corporate governance as a whole is a fairly fragmented discipline (Aguilera & Jackson, 2003). Although there are a number of highly positivistic studies that investigate narrowly defined aspects like board composition and ownership structures, their findings are often inconclusive and lack generalisability (Iwasaki, 2007). In fact, it is difficult to identify a major study within the field that has not been challenged or contradicted. This is explained by the high level of complexity of the corporate governance phenomenon, particularly in an international context (Aguilera & Jackson, 2003). Some suggest that it is impossible to depict the discipline adequately by using a limited number of variables. It is not surprising since such broad areas as culture and individual circumstances play a significant role in determining corporate governance arrangements (Mintz, 2005). Under such conditions researchers often turn to in-depth qualitative investigations of prominent corporate cases and look for theory building opportunities (Fox & Heller, 2000).

Whichever approach is adopted, the test of these studies is their relevance to practice. As suggested by Shleifer & Vishny (1997), research in the area of corporate governance is of enormous practical importance. This practicality of the subject comes from its proximity to core business processes. These processes are to do with the mechanics of decision making (Cuervo, 2002), distribution of residuals (Fox & Heller, 2000), accountability to shareholders (Osugi, 2000), stakeholder management (Moore, 1999), ownership and control (La Porta, Lopez-de-Silanes & Shleifer, 1998), etc. Corporate governance as a subject area is charged with the task of evaluating existing practice and proposing reform solutions (Black, 2001). In this respect, corporate governance runs parallel with the primary objectives of pragmatic research.

### 1.5.1 Russian Context

As far as Russian companies are concerned, corporate governance is a fairly new concept. The Russian economy has gone through a period of rapid change affecting the most fundamental aspects of prevailing business infrastructures (Preobragenskaya & McGee, 2004). The country's transition from command to market economy created an unstable environment in which many companies struggled to survive. It is not a secret that the overwhelming majority of officials engaged in all types of unlawful conduct. Here, the practices ranged from minor administrative violations to criminal offences. This has led to a negative impact on the levels of transparency of Russian corporations. An extremely secretive culture has become a permanent characteristic of Russian enterprises (Fox & Heller, 2000). It is this very fact that has been identified as a stumbling block in most studies of the country's corporate governance.

On a practical level, Russian and foreign companies are becoming more aggressive in seeking out joint-venture opportunities in Russia. This has manifested itself in the rapidly growing number of Initial Public Offerings of Russian companies on the London Stock Exchange and a substantial increase in Foreign Direct Investment over recent years. Hence, the answer to the question of what works and what does not work is constantly gaining practical relevance since the levels of foreign engagement in the country are reaching unprecedented levels (EU-Russia Roundtable on Corporate Governance, 2006).

To summarise, this study is conducted from the philosophical stance of pragmatism. Here, the justification for avoiding a clear-cut commitment to a particular methodology takes its grounding in the following:

- The fragmented nature of the discipline
- The difficulties associated with accessing information
- The usefulness of findings as the overriding objective

The core philosophical underpinning of this work constitutes a call to concentrate more on coping with the world rather than representing it.

## 1.6 Mixed-Methods Research

Mixed-methods research is consistent with the pragmatic view of the world in that it supports paradigm integration along the methodological continuum (Johnson, Onwuegbuzie & Turner, 2007). Typically, mixed-methods research seeks to combine quantitative and qualitative methods in the pursuit of either triangulation or complementarity. Traditionally, mixed-methods research has been viewed as an equal split between qualitative and quantitative inputs. Here, a positivistic questionnaire followed by a series of unstructured in-depth interviews is a commonly used combination.

However, this research has a dominant qualitative component primarily determined by the chosen method of analysis<sup>19</sup>. In fact, quantitative input is limited to descriptive statistics of qualitative data. Mixed methods as a research paradigm does not disallow leaning towards one of the extremes of the methodological continuum. Johnson, Onwuegbuzie & Turner, (2007, p. 124) propose a qualitative dominant sub-type of mixed-methods research where 'one relies on a qualitative, constructivist-post-structuralist-critical view of the research process, while concurrently recognizing that the addition of quantitative data and approaches are likely to benefit most research projects'. This definition of mixed-methods is applied to this study. However, it is necessary to emphasise that the quantitative input is built on and serves the purpose of assisting what is primarily a qualitative analysis.

## 1.7 Research Quality

With regard to the study of corporate governance, it has been suggested that the quantitative approach restricted by the traditional parameters of quality (validity, reliability, replicability) failed to produce conclusive findings in transition economies (Djankov, 2002). This sobering revelation is particularly true in the Russian context (Iwasaki, 2007). The two major surveys of academic studies in the discipline call for a shift in priority to focus more on investigations of less quantifiable aspects of

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<sup>19</sup> The method is termed template analysis (King, 1998); see section 3 of this chapter for further explanation.

the discipline such as the state of institutional construct. In order to address this vital call, it is proposed to re-define quality of research findings in alternative terms. This is a critical point, because the parameters of research quality must run parallel with the underlying philosophical underpinning whilst consistency with the chosen method of data collection and analysis must not be compromised.

The predominantly qualitative nature of this study dictates less statistically bound measures of quality. Mixed methods, along with template analysis, recognize trustworthiness and credibility as acceptable parameters for measuring research quality (Johnson, Onwuegbuzie & Turner, 2007; King, 1998).

### 1.7.1 Trustworthiness

Generally, in qualitative research the burden of inference lies on the researcher (as opposed to statistical tools used in quantitative research) (O'Dwyer, 2004, p. 391). For a long time, this very fact blocked the recognition of this type of enquiry from being regarded as scientifically robust. Nevertheless, qualitative researchers developed an approach that helped them overcome this challenge. This approach manifests itself through the total openness of the research process. Hence, trustworthiness refers to transparency that spans data collection, and more importantly data analysis. Sandelowski (1986) talks about the process of auditability or 'a decision trail' that allows the reader to track and verify the research process. The decision trail serves as a measure of trustworthiness of the findings. Clearly, transparency does not eliminate subjectivity, nor is it its purpose to do so. However, it does reveal the logic applied to every stage of a research project, exposing the mechanics of data collection and analysis (Johnson *et al.*, 2006). It is for this reason that the process of constructing and analysing a template should be presented with a great deal of detail. In the section on template analysis, the process of identifying and analysing templates depicting corporate disputes is not only explained, but also demonstrated using the working papers of the research. Such a detailed disclosure of the study is necessary in order to persuade the reader that the research process is traceable and verifiable. However, this research does not claim to be replicable. Pragmatism does not confine researchers to a search of a single reality, and consequently repeatability

ceases to be 'an essential property' of a trustworthy research (Sandelowski, 1986, p. 3). Nevertheless, it is important to reinforce that 'a study is trustworthy only if the reader of the research report judges it to be so' (Rolfe, 2006, p. 305).

### **1.7.2 Credibility**

Credibility corresponds roughly to the positivistic notion of internal validity (Rolfe, 2006). This measure refers to the accuracy of analysis. In qualitative research, member checks (retuning to participants after data analysis) and peer checks (using a panel of experts or an experienced colleague to re-analyse some of the data) have been regarded as important techniques for increasing accuracy and hence credibility of research (Guba & Lincoln, 1989). Since newspaper articles are the main source of data, this research is complemented by interviews with the Moscow Times reporters. It is important to acknowledge however that the interviews were conducted during the stage of data analysis and therefore cannot serve as a check of accuracy of interpretation outside the concept of triangulation. In this respect, this study strives to achieve credibility through comparing and complementing inferences made from the analysis of articles and interview data. Moreover, since a degree of subjective judgement is an intrinsic part of qualitative analysis, credibility checks must be viewed as study specific rather than something predetermined and universally applicable (Sandelowski, 1993; Rolfe, 2006).

### **1.8 Status of the Findings**

Status of the findings usually refers to the level of generalisability. The proclaimed goal of quantitative research is to achieve total generalisability and reveal the single reality as underpinned by the philosophical concept of positivism. The goal is achieved by ensuring that the sample used is big enough and representative, as well as the method of analysis being chosen and applied correctly. Conversely, qualitative research focuses on individual interpretations as a means of increasing our understanding of more complex social phenomena. The findings are not generalisable, but reveal intricate details of the phenomena under investigation.

The varying degree of generalisability and associated quality checks of the alternative research paradigms are shown on figure 3.3 a.

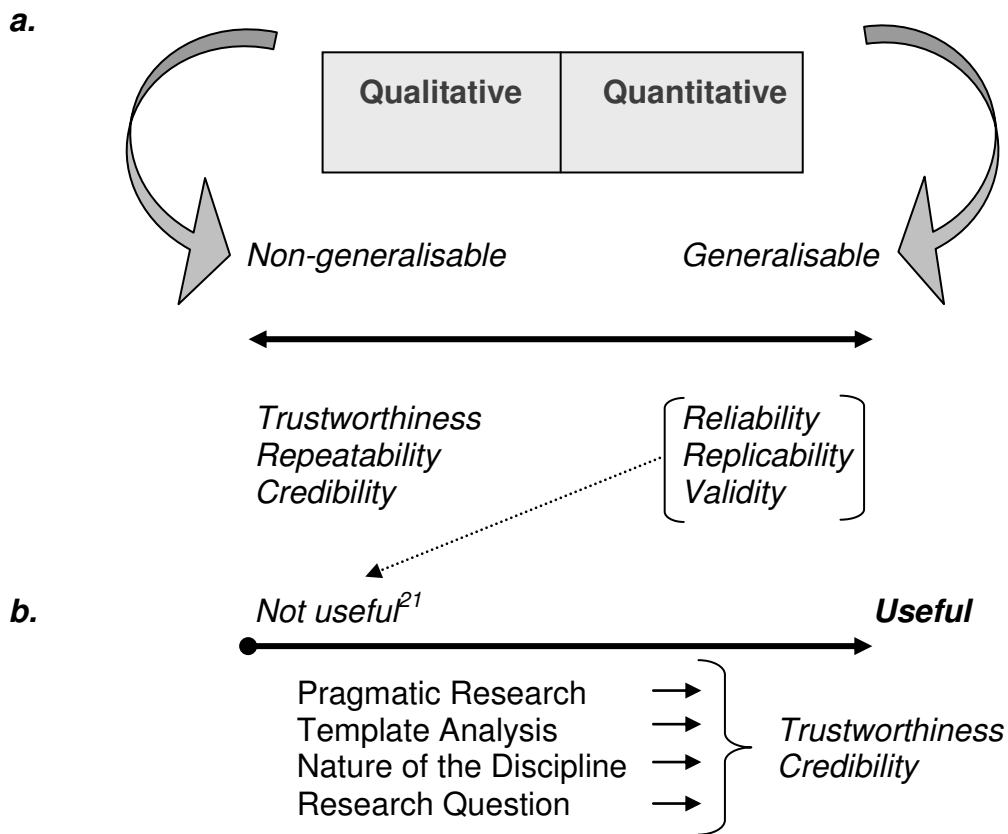
As a rule, most corporate governance studies in the Russian context lean towards the generalisable end of the continuum (Iwasaki, 2007), but have been criticised for their lack of usefulness stemming from the contradictory nature of the findings. The philosophical underpinning of this work helps to solve this dilemma by replacing the '*generalisability continuum*' with the '*usefulness continuum*' which is considered to be the overall indication of the status of the findings (see figure 3.3 b.).

This study seeks to explore the factors at work and to present the findings as examples of agency-based conflicts, and how these have changed with inferences about the balance of power and the rule of law<sup>20</sup>. It has been suggested that lack of the rule of law and unpredictable power structures represent the biggest challenge to Western investors in the Russian context (Black & Kraakman, 1996; Sucher & Bychkova, 2001; Kochetygova *et al.*, 2004). Learning more about the phenomenon is therefore bound to have useful implications which, in the context of this research, serve as a manifestation of the status of findings.

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<sup>20</sup> The author would like to thank Prof. Laura Spira and John Forker for their extremely useful comments on the methodology of this work presented at the Financial Reporting and Business Communication Conference in Cardiff, 2007.

Figure 3.3: *General Status of Findings*



### 1.9 Source of Subjectivity

Holloway & Wheeler (1996, p. 10), describe qualitative research as “holistic, emic, contextualized, interpretive, and immersed”. Within the discipline of corporate governance, this framework is very well positioned to contribute to the practical dimension of research outcomes. It is clear that the subjective element is an integral part of the aforementioned characteristics of qualitative research and therefore needs to be revealed.

The first source of subjectivity within this research relates to the primary method of data collection. In general, newspaper sources have been frequently used in event analysis. The reason for this is the fact that other sources of data are likely to

<sup>21</sup> There is no suggestion that quantitative research has no place in the study of corporate governance. However, there is evidence to suggest that the dominance of this line of enquiry in the Russian context produced contradictory findings with limited applicability (Iwasaki, 2007). Furthermore, the diagram does not propose that reliability, replicability and validity are undesirable characteristics of the research quality. On the contrary, they are desirable. However, very often strict adherence to these quality checks can force researchers to re-formulate the research question, or drop otherwise legitimate enquiries all together.

contain a larger bias or (as the case is in this particular study) are simply unavailable to most researchers. Nevertheless, newspaper sources pose fundamental problems of a methodological nature. With regard to longitudinal studies, or when two time periods are compared, it is important to know whether press data accurately represents events under consideration, or is skewed by journalists' selection process and a change in reporting practice. Although contamination of newspaper data has been categorically acknowledged (Danzger, 1975), others rather convincingly argue that no alternative source provides 'as complete an account of events as newspapers for the widest sample of geographical and temporal units' (Olzak, 1989, p. 128). Moreover, even in the purely quantitative sense, the bias of newspaper sources has been described as stable and therefore acceptable for formal analysis. The metaphor used by Barranco & Wisler (1999) is that of a thermometer that shows temperature incorrectly. Here, the point is that if inaccuracy is consistent, then we can still learn about the changing nature of the unit of analysis through a systematic comparison. Their study of public demonstrations in Swiss cities confirms the latter proposition which serves as the fundamental justification for the choice of the source of data for this study.

Articles from the Moscow Times, although factual in nature, are primarily informed by Western business people and written by Anglo-Saxon reporters. It is not surprising that a lot of published material on corporate disputes has a certain degree of bias in favour of foreign investors (particularly European and Anglo-Saxon). As a source from the Moscow Times put it:

*"I think the only potential bias you could find in a Moscow Times story is the inevitable pro-foreigner bias that you would find in any foreign newspaper working in Russia. There is always going to be some subtle bias in favour of foreign investors just by the simple fact that they speak our language natively and we understand them better than we do the Russians. But that was never overt and I think we tried very hard to avoid that but I think that's probably a bias you will see in some Moscow Times stories" (see interview guide, appendix 4, question 4).*

It is important to acknowledge that this bias is not accidental, as one of the aspects of this research is to investigate the phenomenon of Russian corporate governance from the perspective of Western investors. This bias very much



contributes to foreigners' perception of the environment and, by virtue of that fact, influences the actual corporate governance practice. Moreover, the bias can be considered inert since it has been confirmed separately and independently by journalists who worked for the newspaper in 1998 and 2006.

An additional consideration here is that relying on a Russian newspaper would have produced a much greater anti-foreign bias. It is a general consensus (among both Russian and Western reporters) that Russian newspapers are subject to a greater degree of political pressure and hence are less free to portray the environment in factual terms and with the same degree of accuracy (Osipovich, 2008).

The second source of subjectivity comes from the interviewees themselves. Clearly, answers to the questions must have been very much determined by the participants' individual experience. In general, reporters are largely free from that bias because they work for the same organisation and are equally well informed about the environment. However, they are still expected to have a varying degree of specialised knowledge and, more importantly, unique experience and circumstances. These circumstances cannot be fully disclosed for confidentiality and anonymity reasons, but are considered while analysing interview data and constructing analytical and concluding inferences.

Moreover, the researcher's bias needs to be acknowledged. This bias spans the whole of the research affecting data collection and analysis. The process of identification of corporate disputes covered in newspaper articles is full of subjective elements. This source of subjectivism revealed in the subsequent sections as the 'decision trail' is exposed. For the purpose of clarity, it is critical to reiterate that the aim of presenting the 'decision trail' is not to ensure repeatability of the study, but to reveal and explain the logic behind each decision made.

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## Section 2: Data Collection

This section explains how the data was collected. It covers both archival material and semi-structured interviews.

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### 2.1 The Moscow Times Archival Data

There has been a considerable level of research using newspaper archives because they ‘incorporate a number of facets concerning a country’s social, political and economic history’ (Gatos *et al.*, 2000, p. 77). Archival data is usually fairly bulky and therefore is typically analysed by means of computer aided techniques. With regard to newspaper archives, quantitative content analysis is widely used to determine the dynamics of narrowly defined social events (Barranco & Wisler, 1999). Text recognition programmes are of key importance in these scientific endeavours.

This research uses The Moscow Times archives as the main source of data. Appendix 1a presents background information about this source of data while appendix 1b contains reporters’ accounts of the paper’s independence and influence.

The website of the newspaper contains a comprehensive search engine which helps to track articles matching a specific description. However, in order to collect all articles about corporate disputes it was necessary to study the content, manually analysing all published material pertaining to 1998 and 2006. Such necessity comes from the fact that it is impossible to describe all disputes by means of a limited number of key words. However, once this time-consuming exercise was complete, the search engine was used to double-check that no article had been omitted.

#### 2.1.1 Definition of Corporate Disputes

The key difficulty in extracting the right articles is determined by a fairly general unit of analysis, i.e. corporate disputes. What constitutes a corporate dispute and what does not may be interpreted differently. The following is the adopted definition of a corporate dispute in the context of this study:

- **A conflict of interests between identifiable/affected stakeholders<sup>22</sup>, typically followed by a resolution.**

Altogether 290 articles<sup>23</sup> depicting corporate disputes matching the above definition have been selected from the newspaper's business section. Clearly, bigger corporate disputes like Shell vs. Gazprom over Sakhalin 2 received a great deal of coverage spanning 25 articles<sup>24</sup>. However, for a dispute to qualify, one dedicated article was considered sufficient. A large proportion of corporate disputes included in the analysis originate from a single article<sup>25</sup>.

Appendix 3 contains an example of a typical article covering a corporate dispute. Having studied the appended article, it is easy to see what is meant by a corporate dispute and how it can be reliably identified even though an all-encompassing criterion for the selection process probably does not exist.

In addition, a number of issues have been identified while collecting articles on corporate disputes:

- Some disputes were covered across a number of articles, whereas others were mentioned in a single issue. Although weightings based on a number of articles covering a dispute are used, articles that repeat previously reported facts have been disregarded.

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<sup>22</sup> The most prominent stakeholders in the Russian context are shareholders, the state, workers' unions, tax authorities and local administration.

<sup>23</sup> 175 articles representing 1998 data and 115 articles pertaining to 2006.

<sup>24</sup> This dispute was very extensively covered by the Moscow Times because of its magnitude. Sakhalin 2 was a \$22 b. investment project.

<sup>25</sup> Analysis of data (chapter 4) provides additional information about the amount of coverage each coded dispute received.

- A dispute covered in the newspaper might have a continuation which was not necessarily covered in the subsequent issues within the two years of the study. Moreover, a dispute may be an ongoing one, i.e. pending resolution. These were recorded and coded according to the data published within the two years under analysis.
- An actual dispute might have taken place prior to the two years under consideration, but for whatever reason was reported later. Articles with such disputes were included in the data because their coverage has an impact on the readers, and hence investor perception of the environment.
- The focus of an article may be other than the dispute itself which is mentioned in passing as a point of reference or a comparison. In these circumstances such disputes were disregarded.

## 2.2 Semi-Structured Interviews

The second stage of data collection is conducted by means of semi-structured interviews. The goal of such interviews is to reveal the research topic from the perspective of the interviewees (Kvale, 1983).

In broader terms, qualitative interviews can be divided into two opposing types. In the first type, the interview situation determines participants' responses (Madill *et al.*, 2000). The content of this type of interview is detached from the participant's personal experience, and for that reason cannot be used as a source of triangulation in events analysis. Conversely, the second type of qualitative interviews enables researchers to learn about participants' experience outside the interview setting and is therefore very much concerned with the accuracy of accounts produced. This type of interview is generally more structured as comparability of accounts must be ensured. This type of data collection has been termed 'realist interviews' (Madill *et al.*, 2000) and is used in this research. The critical point here is that researchers may compare realist 'interview findings with those obtained through other methods, such as documentary analysis' with the purpose of triangulation (King, 2004, p. 12).

Realist interview guides tend to be fairly structured with a more narrowly defined topic for discussion (King, 2004). The interview guide used in this research is presented in appendix 4. The process of developing the questions was very much influenced by the analysis of the newspaper articles and two pilot interviews with industry experts. The latter revealed the need to simplify the questions<sup>26</sup> and focus the interviews solely on the participants' experience/knowledge of corporate disputes in the country. The pilot interviews also uncovered a challenge inherent to the research design, i.e. asking participants to recall a corporate dispute from as far back as 1998. This flaw was overcome by making sure that the interviewees received a copy of the questions well in advance of the interview<sup>27</sup>. Furthermore, in order to provide participants with more flexibility it was decided to refer to the late 1990s rather than specifically 1998. Nevertheless, despite this change in the research design, all of the disputes referred to in the interviews took place in 1998<sup>28</sup> and were covered by the Moscow Times reports.

### 2.2.1 Interviews with the Moscow Times Reporters

Altogether five interviews with the Moscow Times reporters were conducted. Three interviews were with the reporters who worked for the newspaper in 1998 and two interviews were with the reporters who wrote in 2006<sup>29</sup>. The interviewees were chosen on the basis of their contributions to the selected articles in the respective time periods.

With regard to this study, the purpose of the interviews is to triangulate and complement analysis of archival data as well as seek the opinion of the reporters on the newspaper's independence and influence. Even though the number of

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<sup>26</sup> Initially, academic terms like 'institutional construct' and 'extra judiciary enforcement' were used in the interview guide.

<sup>27</sup> Most of the reporters found it useful for interviews to begin with a brief recap of most commonly reported disputes at the time.

<sup>28</sup> The explanation for that could be the 1998 financial crisis that increased the number of corporate disputes and generally made that year particularly memorable.

<sup>29</sup> The reason for including an extra interview for 1998 lies in the fact that participants had difficulty remembering facts from almost a decade ago. By including an extra interview, the impact of this asymmetry with 2006 data was reduced.

interviews is fairly limited, in terms of the combined coverage, interviewed reporters contributed to just under 50% of the articles that had been selected for analysis in the first stage of data collection.

### 2.2.2 Telephone Interviews

Telephone interviews are by no means inferior to face-to-face interviews (Wiseman, 1972). According to Rogers (1976) telephone interviews have a number of compelling advantages. They are:

- less biased towards socially acceptable responses;
- no different in accuracy and completeness in comparison with face-to-face interviews;
- cheaper and easier to arrange.

However, the most commonly cited criticism of telephone interviews is that they deprive the interviewer of an opportunity to interact with the interviewee at the level of engagement offered by face-to-face communication (Rogers, 1976). Furthermore, absence of the visual aspect of communication not only poses challenges to the actual conduct of interviews, but can also lead to a possible loss of data. A lot of signals that facilitate interaction between the researcher and participant in a face-to-face interview are unavailable in a telephone interview situation. Absence of these clues may make it more difficult for researchers to establish the right rapport with their interviewees.

Interviews with all Moscow Times reporters were conducted by telephone. In general, journalists depend on other people's willingness to talk, and therefore tend to be very approachable themselves. Moreover, reporters are very skilled at conducting interviews by phone themselves. This fact made it easier for the researcher to establish a positive rapport with the respondents.

Additionally, all interviews with the reporters were recorded by means of special teleconferencing equipment making it easier to concentrate on the systematic questioning and participants' responses.

### 2.2.3 Transcribing

All recorded interviews were subsequently transcribed with the help of a professional typist. In total, approximately 20,000 words of transcribed material was produced. Subsequently, the text was checked for mistakes by the researcher. This made it possible to eliminate content inaccuracies and typing errors, as well as provide the researcher with an opportunity to become more familiar with the data. Amended transcripts were sent back to the research participants for their comments. Once feedback<sup>30</sup> from the research participants had been received, the final text was subject to proofreading, after which it was deemed ready for initial analysis.

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<sup>30</sup> Feedback primarily constituted additional facts and never serious amendments to the actual content. No comment was withdrawn by any of the interviewed reporters.

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## Section 3: Data Analysis

This section explains the main principles of the chosen method of analysis as it is used in this study. A demonstration of how the coding was conducted is also provided. Additionally, expected original contribution and methodological limitations are presented

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### 3.1 Method of Analysis

This study is concerned with analysis of textual data which may be carried out by means of either content analysis or template analysis. Here, the most significant distinction is not necessarily determined by opposing philosophical underpinnings of the two methods, but manifests itself through the varying degree of procedural restrictions (King, 2004).

The investigation of corporate governance in Russia is dependent upon the researcher's success in gaining access to the relevant data. The external environment makes it extremely difficult to penetrate generally high levels of suspicion and where there is a strong reluctance to sharing information when it comes to the subject matter. Under such conditions, it is very risky to accept restrictive methods of data collection and analysis.

Template analysis has been chosen for the purpose of this study because it allows a great deal of freedom in the application and development of codes while engaging with textual data. It is not prescriptive in terms of epistemological positions (King, 2004) and has been used in pragmatic research. The method offers sufficient scope for the development of useful codes, as it accepts both objective (Miles & Huberman, 1994) and subjective (Madill *et al*, 2000) methodologies claiming these to be subordinate to the interplay between the researcher and data<sup>31</sup>.

Due to such an inherent flexibility, template analysis encompasses a wide range of techniques (King, 2004). Very often these techniques amount to assigning a list of codes to corresponding themes identified in textual data. Related themes are then organised in a template that usually has a hierarchical structure (King, 2004). It

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<sup>31</sup> If applicability of codes is the ultimate aim of such interplay, then the pragmatist criteria is fulfilled.



has to be mentioned that rules with regard to identifying themes<sup>32</sup>, defining codes<sup>33</sup>, and assigning codes to themes are often interpreted differently in the context of various studies because of their general nature. Consequently, descriptions of this method in research methodology literature are fairly brief while a lot of emphasis is placed on the demonstration of how the method was used in a particular study (Symon & Cassell, 2004). The explanation for this lies in the fact that, with regard to template analysis, most researchers have to alter certain aspects of the method based on the nature of the research question and unique characteristics of accumulated data.

This research seeks to capture institutional change through analysis of corporate disputes, and draws on newspaper articles as a major source of data. Therefore, modification of the chosen method of analysis is required in order to fulfil the purpose of this research and accommodate unique characteristics of the data set. This chapter proceeds with the demonstration of how newspaper articles have been transformed into templates that were subsequently used in the analysis chapter of this thesis.

### 3.2 Template Analysis

Template analysis can be applied to any textual data, including newspaper articles, for its capacity to deal with large data sets (King, 2006). However, most frequently this method of data analysis deals with interview transcripts which as a rule address research questions directly. This is not the case with newspaper articles which are originally written for a different purpose. The above section on archival data collection demonstrates how the Moscow Times articles have been selected in order to ensure their relevance. As previously stated, 290 articles (approximately 200,000 words) in total have been subjected to template analysis.

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<sup>32</sup> Themes are features of participants' accounts which characterise particular perceptions and/or experiences which the researcher sees as relevant to the research question (King, 2004).

<sup>33</sup> Coding is the process of identifying themes in accounts and attaching labels (codes) to index them (King, 2004).

### 3.2.1 A Priori Themes

*A priori* themes relating to the nature of corporate disputes (Fox & Heller, 2000) and enforcement strategies (Hendley *et al.*, 1999) have been borrowed from the literature. Dispute-related themes were also complemented by additional themes that were developed further to a comprehensive review of the Russian law on joint stock companies that rather specifically defines potential areas of conflict. Furthermore, the 'other' category in relation to corporate disputes and enforcement strategies have been added to ensure that preliminary coding erred on the side of inclusivity. All *a priori* themes are presented in appendix 6 a.

### 3.2.2 Developing Themes

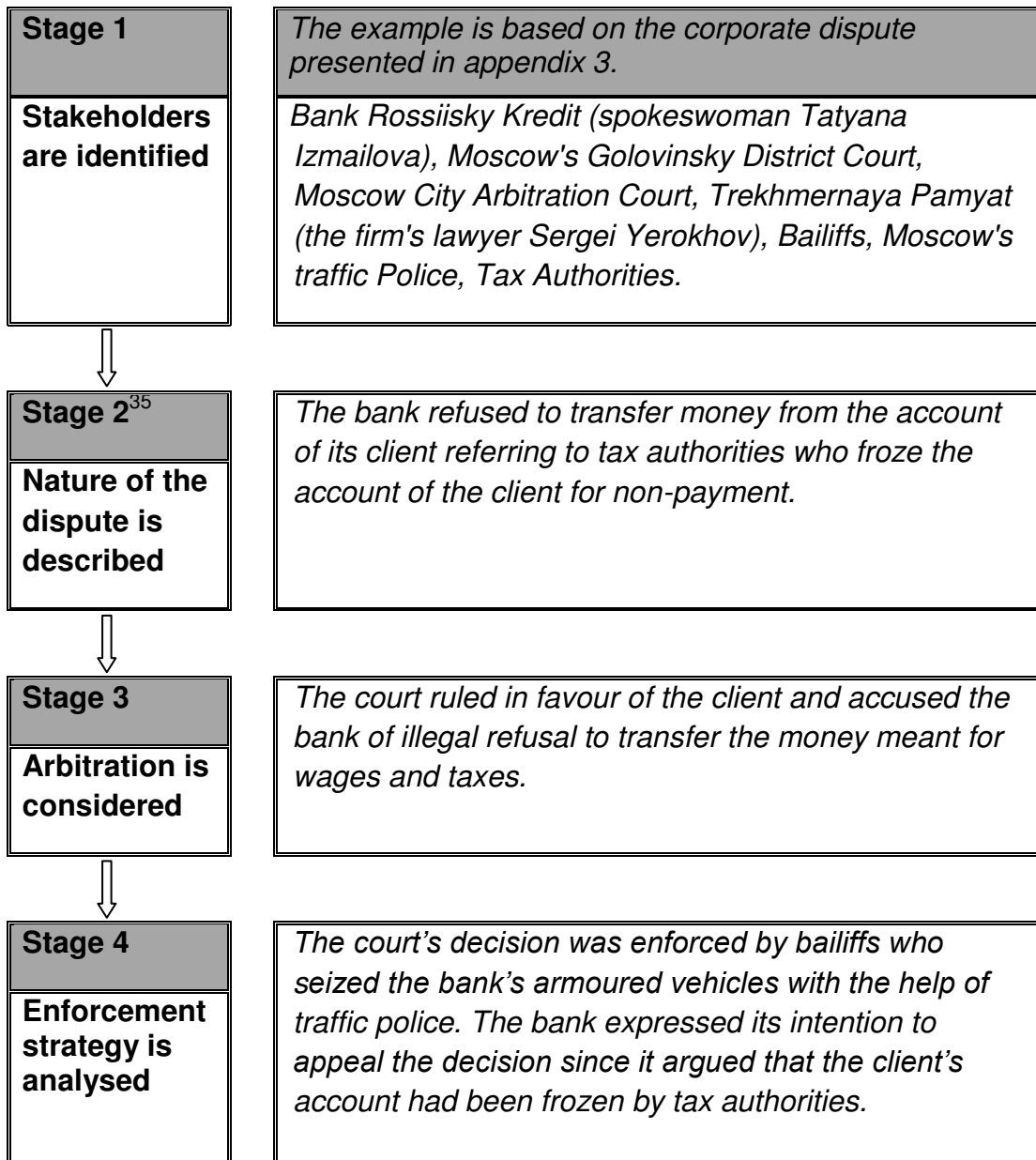
*A priori* themes proved to be relevant to the content of the Moscow Times articles on corporate disputes. However, further development of the themes was required in order to capture the richness of the newspaper accounts while ensuring that a meaningful grouping of the themes was still possible. Changes to *a priori* themes are presented in appendix 6b.

It has to be acknowledged that the process of developing the themes was fused with subjectivity. Without seeking to eliminate the latter, understandable concerns over research rigour can be addressed by a demonstration of how disputes were recorded and themes identified prior to the coding process (see figure 3.1 which presents a four-step<sup>34</sup> example based on the corporate dispute described in appendix 3).

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<sup>34</sup> The four steps have been determined by the adopted definition of corporate disputes. For a dispute to qualify for the study the content of selected articles would normally outline key stakeholders, nature of the dispute, arbitration and enforcement.

Figure 3.4: *Example of how disputes were recorded*



Once every dispute had been recorded in this way, it was possible to see which *a priori* themes best captured the data and which themes needed to be expanded, altered or excluded. With regard to the above example, the following themes were identified:

<sup>35</sup> Although every effort was made to ensure that steps 2, 3 and 4 reflect the content of the articles, they are descriptions produced by the researcher and in this respect are not bias-free.

- Diversion of claims: refusal to transfer money to customer
- Litigation: a court ruling in favour of the customer enforced by bailiffs who seized property of the bank.
- Unclear rules: the bank appealed the decision of the court claiming that the client's account had been frozen by tax authorities.

Following Fox & Heller (2000) (see appendix 2), it was necessary to expand the definition of the 'diversion of claims' pathology to include disputed instances of non-payment. Moreover, emerging themes such as unclear/contradictory/inadequate rules had to be added to the list of themes in order to capture more specific aspects of corporate disputes.

In developing the themes it was necessary to retain the balance between a comprehensive structure and applicability to the data set. In other words, it was important to ensure that the content of the selected articles was covered fully by the final themes with an appropriate level of detail<sup>36</sup>. This reflects on the task of data collection and explains the strategy adopted for the development of the *a priori* themes.

### 3.2.3 Coding

Once definitions had been attached to each theme, it was necessary to arrange the data in a way which would be conducive of a detailed analysis. King (2004) advocates a hierarchical structure of arranging data. This hierarchical structure is created by allocating 'higher order codes' to the most general themes while more narrowly defined sub-themes are attached to 'lower order codes'. While reviewing definitions of each theme, a 3-order hierarchy depicted in table 3.1 emerged.

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<sup>36</sup> Once this condition was met, the two 'other' categories became redundant.

Table 3.1: *Coding Corporate Disputes*

<b>First Order</b>			
Management	<b>1.1</b>	Diversion	<b>1.2</b>
<b>Second Order</b>			
1. Bankruptcy	<b>1.1.1</b>	1. Diversion of Assets	<b>1.2.1</b>
2. Ownership	<b>1.1.2</b>	2. Diversion of Claims	<b>1.2.2</b>
3. Misinvestment	<b>1.1.3</b>		
4. Misimplementation	<b>1.1.4</b>		
5. Taxes	<b>1.1.5</b>		
6. Control	<b>1.1.6</b>		
<b>Third Order</b>			
<i>Disputes</i>		<i>Resolution</i>	
<b>D</b>		<b>ES</b>	
1. State Interference		6. Relationship-Based	
2. Inadequate Information		7. Self-Enforcement	
3. General Meetings		8. Third-Party Enforcement	
4. Unclear Rules		9. Private Enforcement	
5. Transactions with Self-Interest		10. Administrative Levers of the State	
		11. Shadow of Enforcement	
		12. Litigation	

- **First Order Codes**

All recorded disputes could be divided into two very broad categories: disputes to do with the way companies are managed and disputes that arise as a result of misappropriation (or diversion of funds and assets). This distinction resembles Fox & Heller’s grouping of ‘non-maximisation of residuals’ and ‘non pro-rata distributions’ pathologies. However, in this research the codes correspond to the themes that are defined by the content of the articles, and therefore *a priori* themes used at the initial stage of the analysis became redundant once they fulfilled the purpose of assisting the initial stage of coding.

- Second Order Codes

The second order codes reveal the asymmetric structure of the hierarchy. Managerial disputes are subdivided into 6 codes while diversion disputes consist of only two. As far as template analysis is concerned this asymmetry does not pose a problem because the coding is not supposed to be predetermined, but is created by the researcher himself while engaging with the data. At this stage it is important to state that parallel coding was employed in the analysis of the data (King, 2004). The same dispute could be coded as both e.g. diversion of claims and misinvestment. This fact detracts from the meaningfulness of citing the frequency<sup>37</sup> of a particular type of dispute, but contributes positively to the level of detail with which templates capture reported data.

- Third Order Codes

The purpose of the third order codes is to capture intricate details of the data set. Altogether, there are 12 sub-categories corresponding to each second order code. The first five codes (1-5) further define the nature of the corporate disputes, while the latter seven (6-12) cover the resolution process. Nevertheless it was necessary to limit the hierarchy of data to three levels<sup>38</sup> in order to avoid unnecessary complexity of final templates and ensure that every code is represented by a prominent and easily identifiable theme.

Referring back to the corporate dispute presented in appendix 3, table 3.2 provides an example of a final template of the dispute.

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<sup>37</sup> Template analysis cannot relate frequency to salience (King, 2004).

<sup>38</sup> Level of detail recommended by King (2004).

Table 3.2: *Final Template*

<b>Coding Profile</b>	<b>Theme</b>	<b>Brief Notes</b>
1.2 First Order	Diversion	Disputed transaction
1.2.2 Second Order	Diversion of Claims	Refusal to transfer money to a customer
1.2.2.4 Third Order	Unclear Rules	The bank appealed the decision of the court claiming that the client's account had been frozen by tax authorities
1.2.2.12 Third Order	Litigation	Court ruling was enforced by bailiffs who seized property of the bank

Such a template has been compiled for all disputes extracted from the Moscow Times articles pertaining to 1998 (79 templates) and 2006 (41 templates). All the codes have been entered into a spreadsheet and represent the data for descriptive statistics.

The reason behind not looking beyond the years in question stems from the fact that the study focuses on the investigation of the change in perception. Two clearly defined 'snap shots' of the environment at different points in time will act as an accurate measure of the change in perception provided the 'snap shots' are representative vis-à-vis reported material published in the respective periods under consideration. A year's worth of reported material on corporate disputes is considered representative of the newspaper's coverage for a particular period because of the large number of articles meeting the selection criteria (175 articles representing 1998 data and 115 articles pertaining to 2006). In this respect, expanding the data set is considered unnecessary because an accurate enough representation of the environment can be constructed on the bases of the available data. Additionally, it is important to note that some larger disputes in the study took longer than a year to resolve. However, these disputes were not followed through for two reasons:

1. Larger disputes tend to be resolved in distinct stages which, if match the respective period of reporting, are included in the study. The net impact of these disputes on perception is less than reported material on smaller disputes because the latter are a more significant characteristic of collected data.
2. Some particularly large disputes span over a considerably longer period of time than a year (e.g. Yukos dispute began in 2003 and was not resolved until 2007). In this case, the systematic characteristic of the data needs to be maintained through a clear cut-off point even though some data is inevitably lost as a result. The justification for this lies in the comparative dimension of the final data set that forms the foundation for conclusions about the change in perception with reference to concrete stages of the development of corporate governance in Russia.

### 3.2.4 Semi-Structured Interviews

The purpose of having two sources of data is not so much to increase generalisability of the findings, but to improve credibility of the study. According to Goldkuhl (2004), "*For a pragmatist ... triangulation of sources and methods, are ways to escape a too large dependence on informants' conceptions*" and thus the issue about the nature/quality of inferences is addressed.

Unlike newspaper articles, interviews address the research questions directly. The purpose of semi-structured interviews in the context of this research is to triangulate the coded data<sup>39</sup> as well as to investigate the status of the Moscow Times articles with regard to the accuracy and influence of published material.

Dispute-related questions (see appendix 4, questions 1-3) have been covered by interviews with the newspaper reporters. The coding profiles described above have been created for all disputes covered in such interviews. Constructed templates were then compared for consistency with the templates informed by

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<sup>39</sup> It is important to be sure that no major corporate dispute has been omitted from the coded data and indeed the reported material in general.



newspaper articles. Such a comparison is regarded as central to the task of improving the quality of data, inferences and credibility of the findings.

In order to capitalise on the richness of interview data, all interviews with the Moscow Times reporters have been screened repeatedly for additional information, particularly with regard to more general comments on the changing nature of the rule of law. Although, these comments are excluded from the formal analysis, they played an important role in setting the scene for a comprehensive discussion of the findings.

Questions about the Moscow Times reports (see appendix 4, questions 4a and 4b) were analysed separately. The key themes here had been predetermined at the questioning stage and refer to the levels of accuracy, independence and influence of the newspaper's coverage of corporate disputes in the country. Due to the fairly specific nature of the questions and a limited number of interviews, it was possible to attribute all relevant transcript extracts to the specified themes (see chapter 4 section 5). The purpose of this is to strengthen credibility of the archival data by analysing comments about the articles' accuracy and influence.

### **Original Contribution**

This study strives to analyse the changing nature of the corporate governance environment in Russia. The unique element here is the focus on corporate disputes as a determinant of the institutional infrastructure in the country. Inferences about the change in the environment are informed by a detailed comparison of agency based conflicts and methods of their resolution pertaining to 1998 and 2006. Such a comparison of corporate disputes has not been carried out before.

Methodologically, this study relies on the Moscow Times archives as a main source of data. This source has been used in the study of corporate governance in Russia (Fox & Heller, 2000). However, this investigation not only adds a comparative dimension but also attempts to improve the quality of inferences by

employing template analysis as a technique for a structured, yet holistic, examination of the large data set. Thus, useful amendments to existing frameworks are suggested while the vital call to investigate the role of the institutional construct in the discipline of corporate governance (Iwasaki, 2007) is addressed.

In summary, this study offers original contribution to knowledge because it:

- uses corporate disputes as a unit of analysis
- provides a comparative dimension to the study of institutional environment
- relies on uniquely constructed archival data
- proposes useful amendments to the existing theoretical frameworks
- investigates the way template analysis can be employed in the study of corporate governance.

The practical, theoretical and methodological innovations used in this study contribute to the understanding of the system of corporate governance in Russia leading to greater awareness of the environment while establishing strategically important partnerships. Original contribution of this study is further discussed in chapter 5 (5.4).

## **Limitations**

This study has a number of limitations that need to be acknowledged and addressed through a vigilant analysis and cautious conclusions. This chapter concludes with a summary of these limitations and steps taken to overcome some of them.

### **The Moscow Times Articles:**

- Between 1998 and 2006 the Moscow Times employed several editors
- The physical layout of the newspaper and its website changed
- The situation with regard to the freedom of media in Russia changed
- Newspaper articles can be rather subjective

- A dispute covered in the newspaper might have a continuation which is not necessarily covered in the subsequent issues within the two years of the study
- Some disputes are covered repeatedly (across a number of articles), whereas others are mentioned only in a single issue
- There is a difference between the number of disputes that actually occurred and those that were reported in the newspaper.

In order to overcome these limitations a number of steps have been taken:

1. Some of the limitations above were addressed through interviews with the reporters of the Moscow Times. The interviews revealed that changes of the editors and format of the newspaper did not have a noticeable impact on the reporters' work, particularly in the business section. Additionally, as discussed later in chapter 4 section 5, the growing concern about the freedom of speech in Russia did not apply to the newspaper because of its relatively limited readership.
2. Opinionated articles are included in the data set, because they also determine perceptions about the environment. However, conclusions drawn from the data accept the bias in favour of foreign investors. This point is discussed further in chapter 4, section 5.
3. It is understood that the selected corporate disputes might receive more coverage outside the time scale of this study. Nevertheless, it is still reasonable to disregard this coverage in order to maintain a clear comparative dimension.
4. The intensity of coverage (number of articles per dispute in a given year) has been included in the formal analysis in order to address the associated limitation.
5. The limitation connected with how fully the newspaper represents the environment has been partially addressed through confining the major conclusions to the change in perception.

**Interviews:**

- The interview guide was still at the stage of development when the initial interviews took place
- Some reporters had difficulty recalling corporate disputes from 1998 and consequently, more general questions about the rule of law dominated such discussions.

In addressing limitations connected with the quality of interview data, the following steps were taken:

1. The brief did not refer to any particular disputes and the reporters were asked to recall the most representative disputes.
2. The reporters were asked only about the disputes that took place at the time they were working for the newspaper.
3. The list of questions (appendix 4, excluding the probes), where possible, was sent well in advance of the actual interviews.

**Analysis:**

- Content of constructed codes is descriptive in that it is the researcher's own account of the reported data.

In addressing this limitation, the content of the final templates (appendices 9a and 9b) is presented with the maximum degree of detail. Moreover, the process of constructing the templates described in the chapter was strictly adhered to.

## Chapter Summary

This chapter presented information about the philosophical stance of the researcher and explained the way in which data was collected and analysed. Here the concept of pragmatism was discussed in conjunction with key aspects of the data and template analysis. Additionally, original contribution was discussed in methodological terms. Finally, an outline of limitations and possible solutions was considered.

This chapter provided the framework (in the broadest sense of the word) within which the subsequent analysis and findings need to be considered. It is important to reiterate however, that this is a predominantly qualitative piece of research. Hence, the numerous graphs presented in the next chapter are the constructed representations of the data set the primary purpose of which is to lay out the analysed material in a transparent and structured manner.

## CHAPTER 4: DATA ANALYSIS

### Introduction

The main objective of this chapter is to present the data pertaining to the two periods under investigation (1998 and 2006). First, the reported data is analysed followed by a structured overview of interview material. The key characteristic of this chapter is the comparative dimension which is informed by the constructed templates. Altogether there are five sections. Section 1 comprises a brief outline of the codes and themes based on numerical representations. Section 2 contains a detailed comparison of the second order codes (bankruptcy, ownership, misinvestment, misimplementation, taxes, control, diversion of assets and diversion of claims). Sections 3 and 4 present the information about the third-order codes which further define corporate disputes (state interference, inadequate information, general meeting, unclear rules, and transactions with self-interest) and resolution practices (relationship-based, self, third-party and private enforcements as well as administrative levers of the state, shadow of enforcement and litigation). The ongoing commentary is about how the nature of reported disputes and methods of their resolution evolved over the period under consideration. Section 5 deals with the interview material and presents the results of the triangulation of the data set.

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## Section 1: Numerical Overview of Coded Data

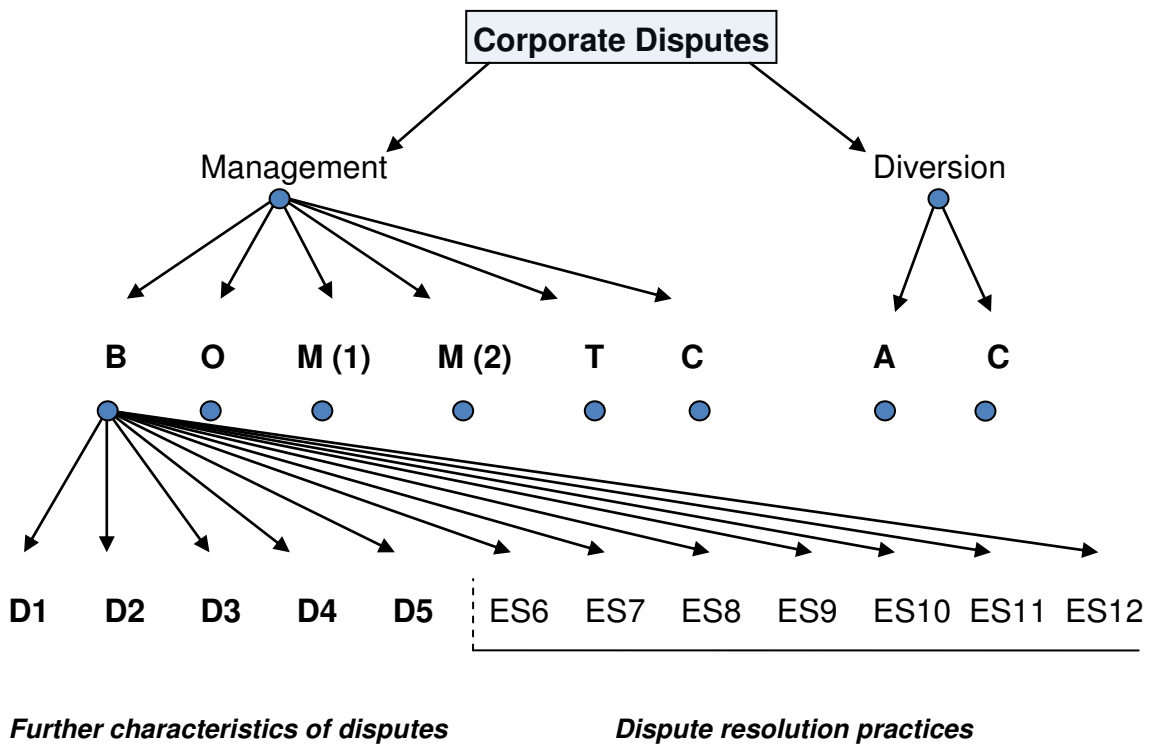
This section provides a numerical overview of coded data representing reported corporate disputes.

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### 1.1 Outline of Codes

Each reported dispute has been allocated to a corresponding code<sup>40</sup>. Additional features of disputes have also been captured by lower order codes. This coding process is central to the way data has been recorded and analysed in this study. The diagram below presents the full hierarchy of codes that has been developed during this research.

Figure 4.1: *Hierarchy of Codes*



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<sup>40</sup> Initially, the codes were informed by themes taken from the literature.

<p><b>Management</b></p> <p>B – Disputes featuring bankruptcy</p> <p>O – Ownership-related disputes</p> <p>M (1) – Misinvestment</p> <p>M (2) – Misimplementation</p> <p>T – Disputes featuring taxes</p> <p>C – Control-related disputes</p> <p><b>Diversion</b></p> <p>A – Diversion of Assets</p> <p>C – Diversion of Claims</p>	<p><b>Lower Order Codes</b></p> <p>D1 – State Interference</p> <p>D2 – Inadequate Information</p> <p>D3 – General Meetings</p> <p>D4 – Unclear Rules</p> <p>D5 – Transactions with Self-Interest</p> <hr/> <p><b>Resolution</b></p> <p>ES6 – Relationship-Based</p> <p>ES7 – Self-Enforcement</p> <p>ES8 – Third-Party Enforcement</p> <p>ES9 – Private Enforcement</p> <p>ES10 – Administrative Levers of the State</p> <p>ES11 – Shadow of Enforcement</p> <p>ES12 – Litigation</p>
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It is critical to reiterate that the above codes are defined by their content rather than a predetermined criterion. In this regard, meaningful analysis needs to follow a certain structure, yet account for the highest possible level of detail. To address this consideration, the analysis chapter begins with a comparative overview of numbers representing types of corporate disputes from 1998 and 2006 and proceeds with a detailed analysis of the content of constructed templates.

The figures behind graphs presented hereunder must be interpreted with a number of limitations in mind. Firstly, this study relies on reported data, and therefore it is impossible to extend applicability of the identified trends to anything other than the change in perception. Secondly, use of parallel coding reduces the relationship between frequency and salience considerably. Thirdly, the figures reflect coverage of corporate disputes produced by a single newspaper, albeit the only one available for the purposes of this study. Evidently, generalisability of such findings is limited. Nevertheless, a numerical overview of reported disputes is possible because it reflects entire coverage of the newspaper and serves as a helpful demonstration of key trends within the sprawling data set.



## 1.2 Corporate Disputes

In 1998, 45 companies spanning 17 industries were reported<sup>41</sup> by the Moscow Times as being party to a corporate conflict. This is in comparison with only 20 companies representing 7 industries in 2006 (see appendices 7a and 7b). The number of articles covering corporate disputes also decreased from 175 in 1998 to 115 in 2006. This reduction is not as drastic as the reduction in the number of companies which suggests that in 2006 a number of larger (in terms of coverage) disputes were reported by the newspaper.

## 1.3 Graphs and Tables

In 2006 the Moscow Times reported fewer corporate disputes than in 1998 (see graph 4.1). In total, 98 separate disputes were featured during the first year of the investigation in comparison with 58 disputes in 2006. Clearly these numbers need to be interpreted in the context of a fairly subjective method of coding. Nevertheless, such a significant difference in numbers reveals a very important trend<sup>42</sup>.

Based on this data it is impossible to conclude whether the corporate environment in Russia has become more or less favourable for foreign investors. To draw a trustworthy conclusion on this point it is necessary to consider the nature of reported corporate disputes which will be done later. However, this data can serve as an indication of an improvement in terms of the way the environment is perceived. This conclusion is based on an underlying assumption that each time a new corporate dispute is reported it has a negative impact on the way investors perceive the environment. At the same time it has to be noted that perception is

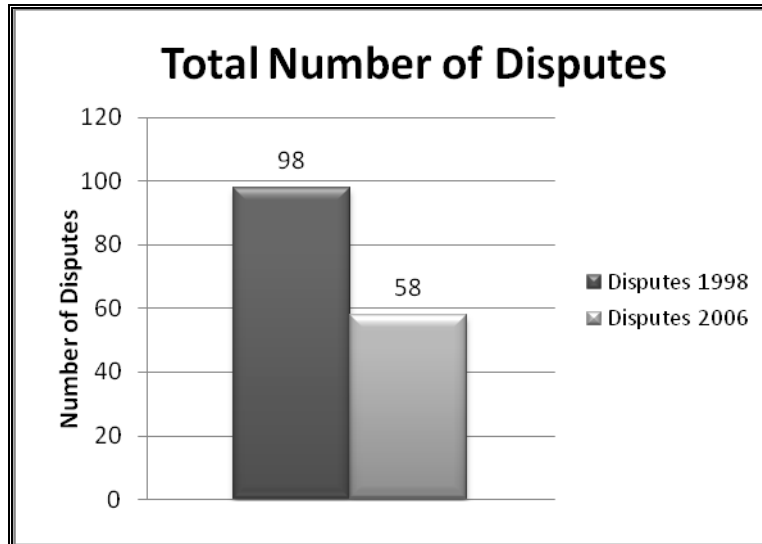
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<sup>41</sup> In order for a dispute to be included in the analysis, it had to be a prominent part of at least one full article.

<sup>42</sup> Validity of the numbers is justified by the fact that all reported material published in the newspaper during the two years under investigation has been screened for corporate disputes. In addition, replicability of these findings is a function of the logic employed at the coding stage.

more closely related to the intensity of coverage rather than the variety of disputes and companies<sup>43</sup>.

Graph 4.1: *Total number of reported corporate disputes*



### 1.3.1 First Order Codes

First order coding divides corporate disputes into two broad categories:

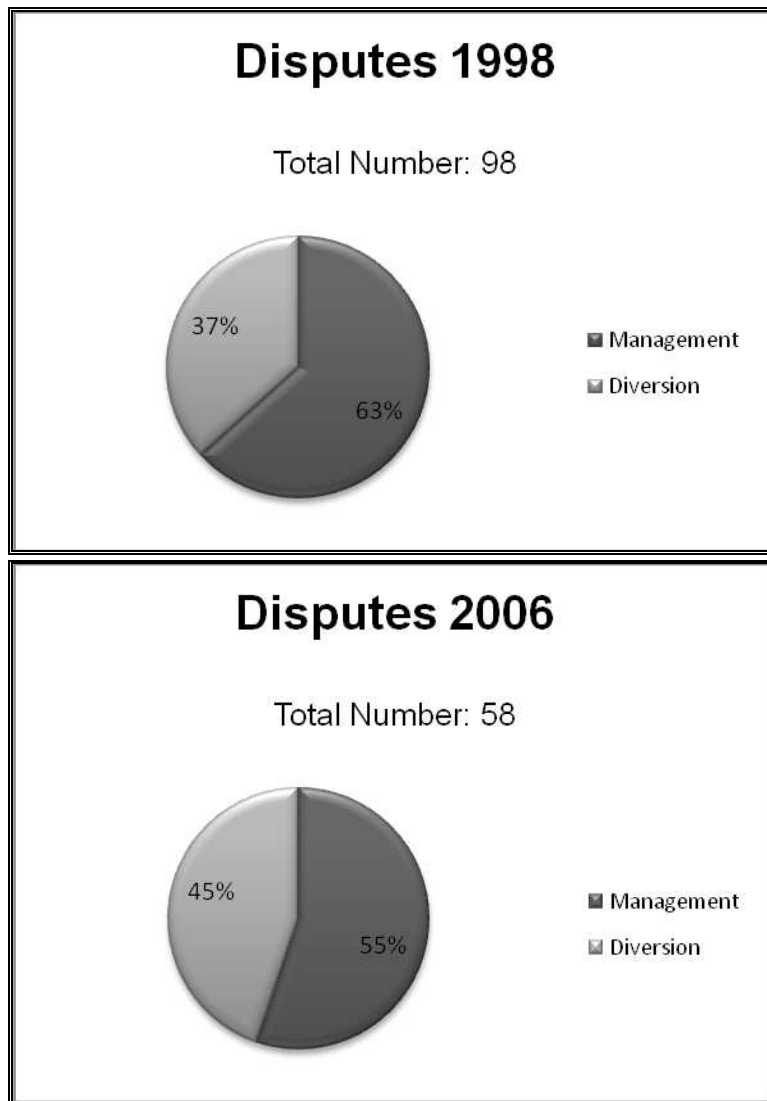
1. Disputes to do with the way companies are managed.
2. Disputes arising as a result of questionable distribution of property and claims.

It has to be recognised that both types of corporate disputes can produce the same outcome, in that a legitimate party's interests are misrepresented. However, if a dispute is coded as a diversion, it implies an outright intention to misappropriate (or steal) by one of the parties to the conflict. Managerial disputes are more of a function of the situation that a company finds itself in. If a corporate dispute contains a feature of more than one theme, parallel coding is employed.

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<sup>43</sup> For that reason it is important to repeat the fact that overall considerably fewer articles covering corporate disputes were published in 2006 than in 1998.

Figure 4.2: Management – Diversion Disputes



The number of both managerial and diversion disputes reported in 1998 exceeded that of 2006 (36 versus 26 instances of diversion and 62 versus 32 conflicts of managerial nature). As depicted in figure 4.2, proportionately, the composition of corporate disputes changed in favour of diversion disputes in the most recent year (45%). Nevertheless, disputes of a managerial nature represent a majority with reference to both years under investigation. The latter point subtly suggests that according to reported data companies find themselves in situations of (potential) danger and that, to a noticeable extent, it is more of a fault of the environment rather than solely caused by actions of self-centred stakeholders that constitute an action of diversion.

### 1.3.2 Second Order Codes

Second order codes further divide managerial and diversion disputes into 6 and 2 subcategories respectively<sup>44</sup>. Disputes of a managerial nature include the following:

- Disputes arising in connection with bankruptcy proceedings
- Disputes related to property rights and ownership
- Disputes arising as a result of investment in an apparently non-viable project (misinvestment)
- Disputes connected with misimplementation of a viable project
- Disputes related to tax arrears
- Disputes over who controls a corporate entity

Diversion disputes are subdivided into:

- Diversion of assets, i.e. a situation when assets are misappropriated
- Diversion of claims, i.e. a situation when financial resources are channelled away from a legitimate stakeholder

It is difficult to rate these subcategories into more or less detrimental ones as far as the corporate climate is concerned. Hence prevalence of a particular type of a dispute is simply a characteristic of the environment<sup>45</sup> rather than an indication of the overall level of hostility.

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<sup>44</sup> This remains reminiscent of Fox & Heller (1999) categorisation albeit with alterations determined by the coding process.

<sup>45</sup> Such prevalence is expected to be indicative of a gap in the institutional construct.

Figure 4.3: *Composition of Diversion Disputes*

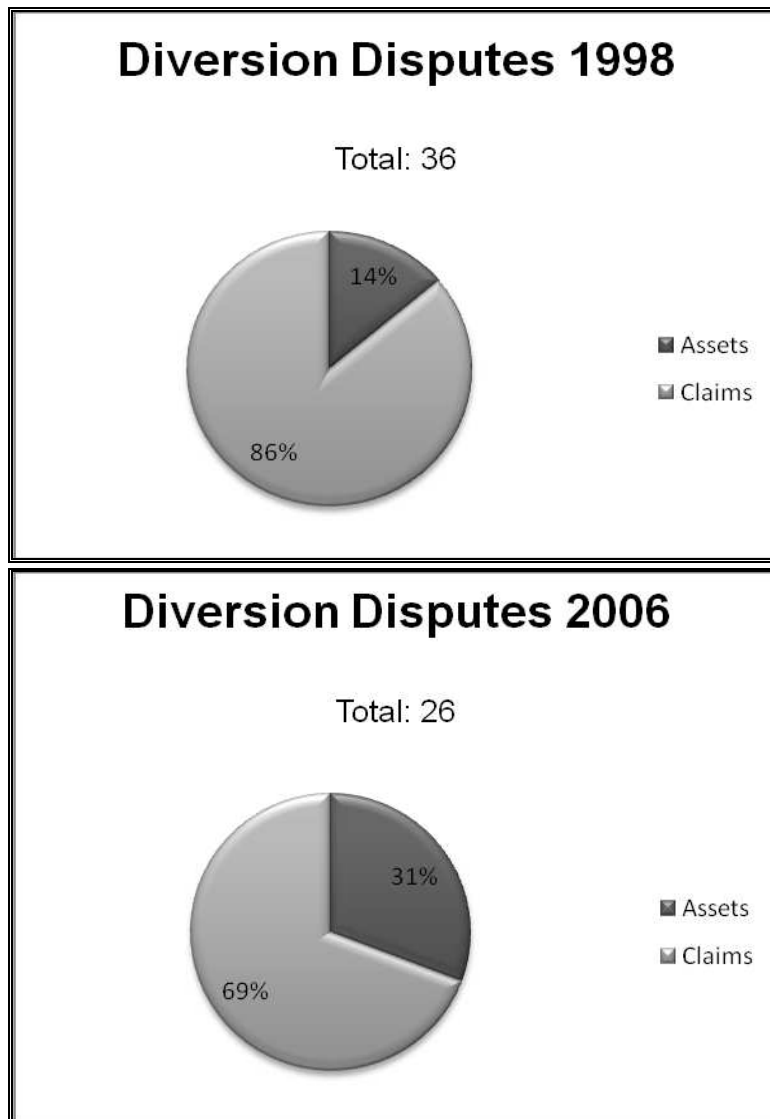
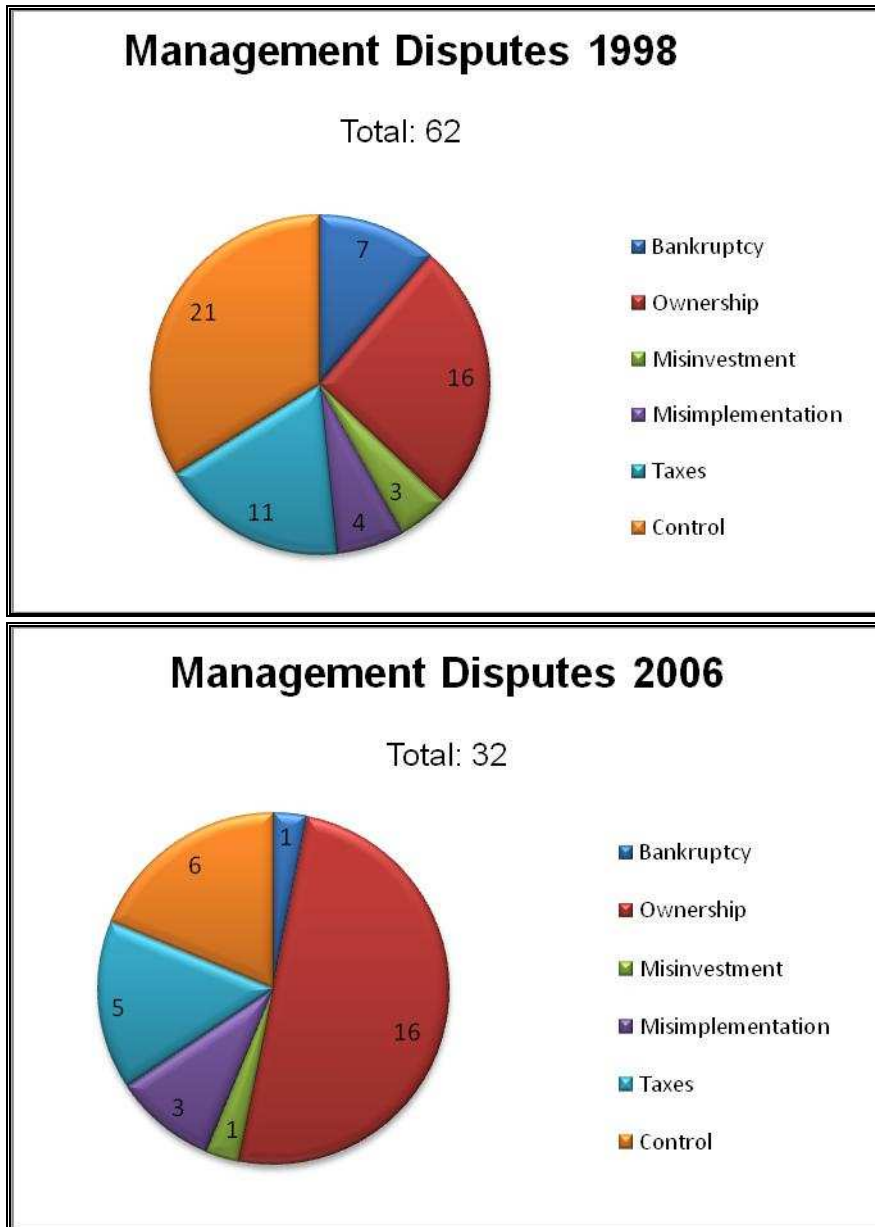


Figure 4.3 shows that despite the significant drop in the total number of corporate disputes, 2006 saw more reported instances of diversion of assets than 1998. This is not surprising in the context of the frequently discussed re-nationalisation of assets within strategic sectors in Russia. Clearly, this figure demonstrates that the re-nationalisation process failed to account for interests of all stakeholders involved leading to a rising number in reported corporate disputes within this subcategory. Nevertheless, an almost twofold reduction in the number of reported disputes coded as diversion of claims suggests a positive change in the form of either more adequate leverage that corporate stakeholders have, or a change in culture that has started to act as a stronger deterrent of outright misappropriation of financial resources. A third explanation behind this perceived trend could be the

fact that individuals in a position of power have accumulated enough wealth and hence have become less aggressive in pursuing financial gains<sup>46</sup>.

Figure 4.4: *Composition of Managerial Disputes*



With regard to disputes of a managerial nature, all the subcategories have witnessed a reduction in the number of reported instances, apart from the ownership subcategory which gave rise to 16 reported disputes in both years

<sup>46</sup> This is a particularly strong deterrent if pursuing more financial gain results in additional risk to legitimacy since it could be safely assumed that in the more recent years such individuals have a great deal more to lose.

under investigation. However, proportionately, this subcategory should be perceived as more dominant in 2006 since the total number of reported managerial disputes fell by 31 instances. Again, this trend is in line with the previous comment regarding the current administration's drive to re-nationalise key strategic assets. However, these figures are not meant to confirm the already known fact of re-nationalisation, but rather clearly suggest that such re-nationalisation took place at the expense of certain stakeholders.

Moreover, disputes over control issues, despite being the most dominant category in 1998, became a less prominent feature of the environment in 2006, both in terms of the total number of reported instances and with regard to proportional representation. This suggests that there has been a positive change in the perceived stability of power structures in the country. This conclusion is drawn on the basis of an assumption that stability of power structures is negatively correlated to the number of reported instances of corporate disputes arising as a result of a struggle for control.

Disputes involving non-payment of taxes and bankruptcy proceedings have again subsided in dominance with the more significant drop in the latter category. This should be the case in an economy where the highly volatile effects of early transition have been largely brought under control. Furthermore, if the overall economic condition of the country has improved, and the existing power structures have strengthened their grip over the majority of assets, then the likelihood of an entity going bankrupt would lessen accordingly. Under such conditions the number of reported instances of bankruptcy disputes is likely to fall. Data extracted from the Moscow Times articles renders support for such a proposition.

According to figure 4.4, misinvestment and misimplementation are the least common forms of corporate disputes as per the Moscow Times coverage. Nevertheless, there were more reported instances when companies failed to implement projects than cases of non-viable investments for the two years covered by the study. Consistent with the overall trend, the number of disputes classified as either misinvestment or misimplementation fell in 2006. It could be argued that this reduction suggests a more shareholder-oriented approach to corporate conduct in Russia since the reduction in the number of reported

instances of these types of disputes can be explained by a greater level of accountability of management to finance providers.

### **1.3.3 Third Order Codes**

As mentioned before, third order codes serve a dual purpose. Firstly, the codes seek to capture further details of reported disputes. Secondly, these codes encapsulate themes related to the style of resolution of captured conflicts.

Graphs 5 and 6 depict dispute-related codes for both years of the study, where there is occurrence of the following:

D1 – State Interference

D2 – Inadequate Information

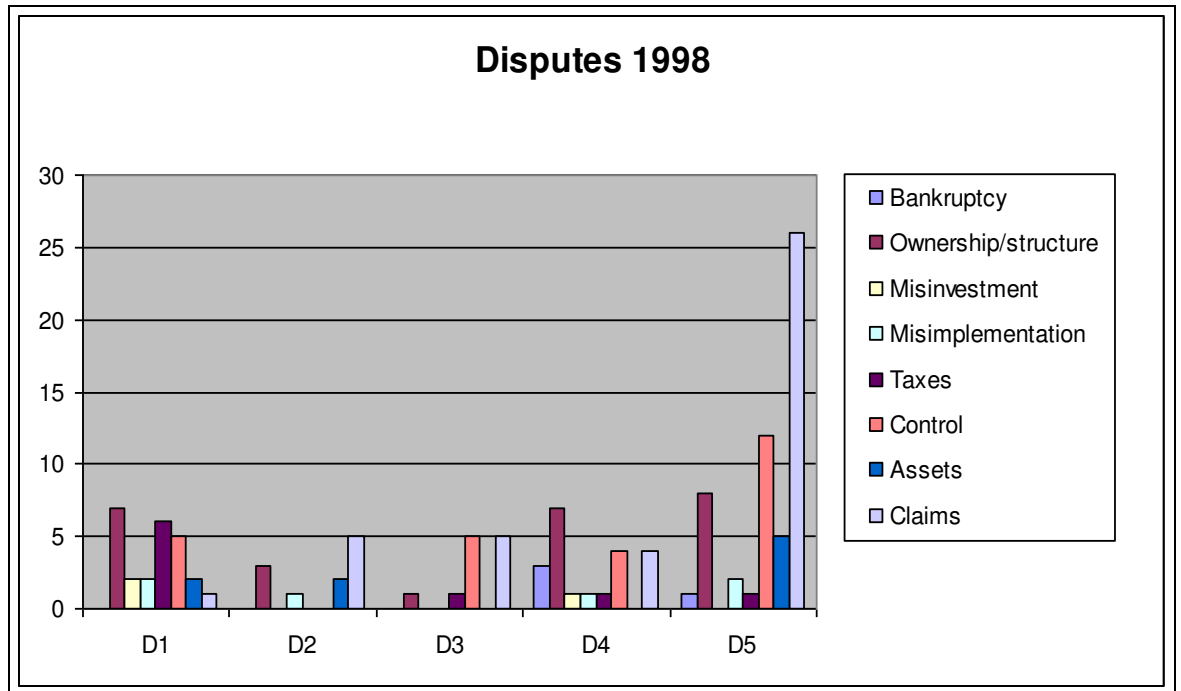
D3 – General Meeting

D4 – Unclear Rules

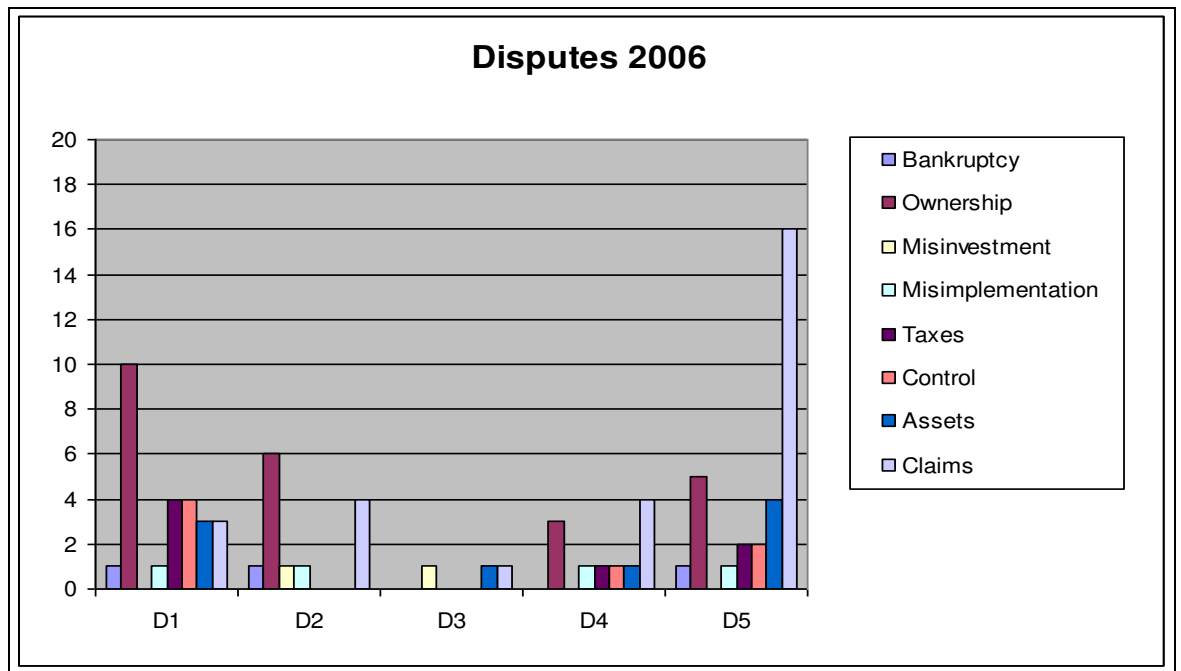
D5 – Transactions with Self-Interest



Graph 4.2: *Sub-types of Corporate Disputes, 1998*



Graph 4.3: *Sub-types of Corporate Disputes, 2006*



The two graphs, apart from summarising all previously discussed trends, also provide an additional dimension represented by the 5 codes.

With regard to state interference (category D1) it can be seen that overall it remains a visible feature of reported corporate disputes. Again with this data, we

are not confirming an already known fact of active state interference in corporate affairs in Russia, but suggesting that such an interference fuels conflicts among affected stakeholders. Additionally, presented figures suggest that corporate conflicts are continuing to be caused by the lack of transparency and poor quality of disclosed information (category D2). However, a subtly positive change occurred with regard to the number of reported disputes featuring general meetings (category D3) and unclear rules (category D4). This could be interpreted as a perceived sign of a more developed framework within which stakeholders negotiate their claims. Finally, with regard to self-centred activities (category D5), although the number of corporate disputes decreased, such a characteristic remains a dominant feature of the reported material covering corporate disputes in 2006.

The second purpose of the third order codes is to capture the changing nature of the resolution process with reference to reported corporate disputes pertaining to the two years of the study, where there is evidence of the following:

ES6 – Relationship-Based Resolution

ES7 – Self-Enforcement

ES8 – Third-Party Enforcement

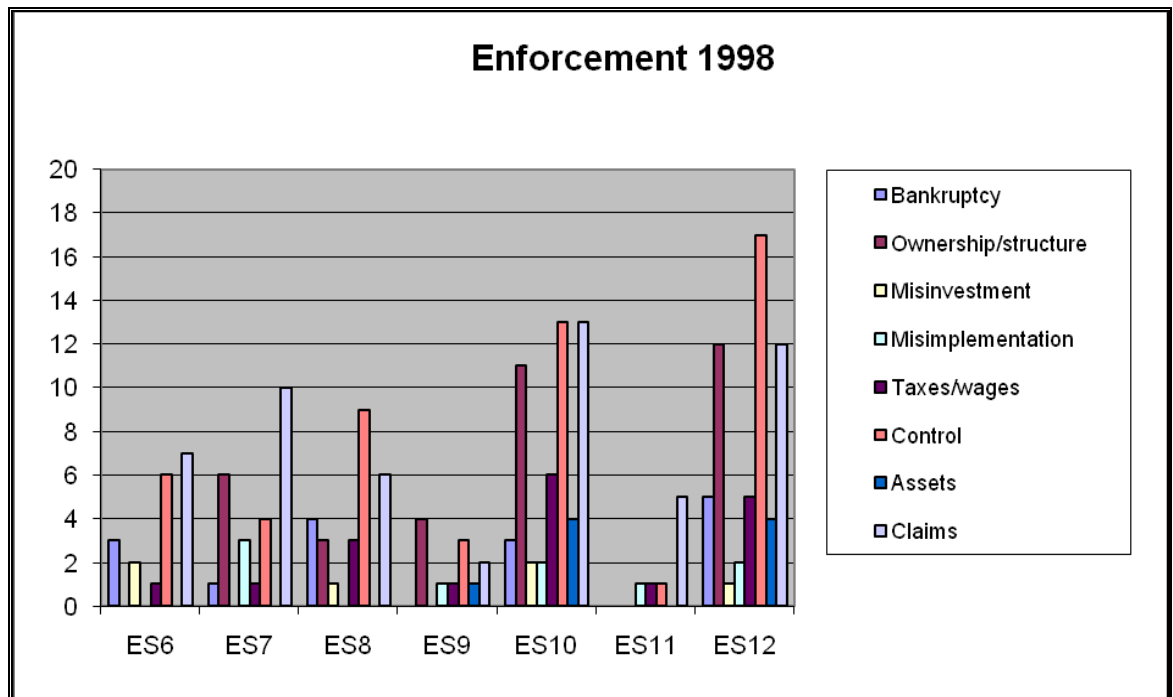
ES9 – Private Enforcement

ES10 – Administrative Levers of the State

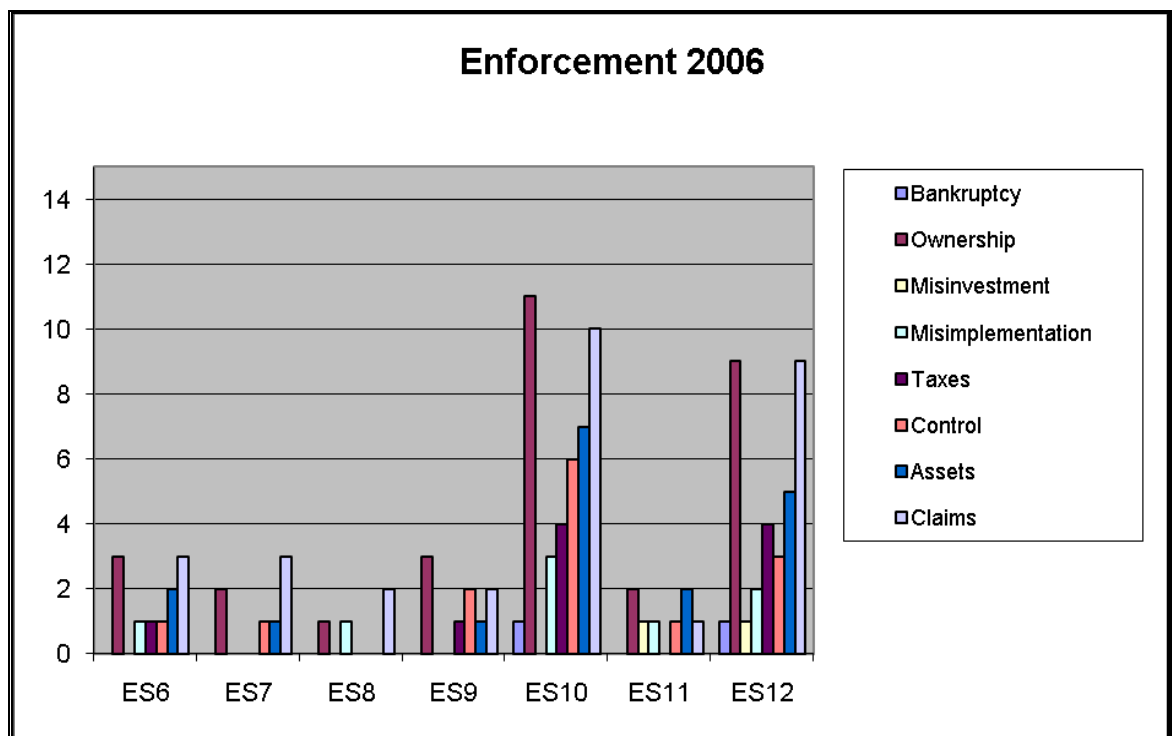
ES11 – Shadow of Enforcement

ES12 – Litigation

Graph 4.4: *Enforcement-related Codes, 1998*



Graph 4.5: *Enforcement-related Codes, 2006*



The two graphs show an apparent dominance of administrative levers of the state and litigation categories. The latter was slightly more prominent in the 1998 coverage whereas the former was more visible in 2006. Considering the overall reduction in the total number of reported disputes, proportionately, these two categories prevail with regard to the 2006 data. In contrast, relationship, self-and

third-party enforcements also featured strongly within the reported material in 1998. A relatively weaker presence of these categories in 2006 indicates a noticeable shift towards a greater involvement of formal institutions in the process of dispute resolution. Again, it is impossible to tell whether or not this shift translated into a fairer resolution process. In order to address this question it is necessary to consider the nature of involvement of such institutions in some detail (this will be done in the subsequent section of the analysis chapter). However, fewer reported instances of relationship, self and third-party enforcement practices should contribute to a change in perception in favour of a gradual development of a more formalised resolution process in the country. Finally, and in contrast with the previous observation, the private enforcement category remained a visible feature of the environment in 2006 according to the Moscow Times data. This category is indicative of the extent of the extra judiciary activity in the country and therefore its largely unchanged presence precludes us from suggesting a positive change in perception with regard to the rule of law in the country at the stage of a general numerical overview of the reported data.

In the following three sections of the chapter the content of constructed templates is presented and analysed in comparative terms. First, the content of second order codes is compared followed by a further scrutiny of more narrowly defined third order codes. Within each subsection specific features of the reported disputes are considered with regard to each theme followed by concluding comments about the perceived change of the rule of law in the country.

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## Section 2: Analysis of the Content of the Second Order Codes

In this section the content of the second order codes is analysed in detail. A graphical representation of each code and relevant themes extracted from the reported disputes are provided for 1998 and 2006.

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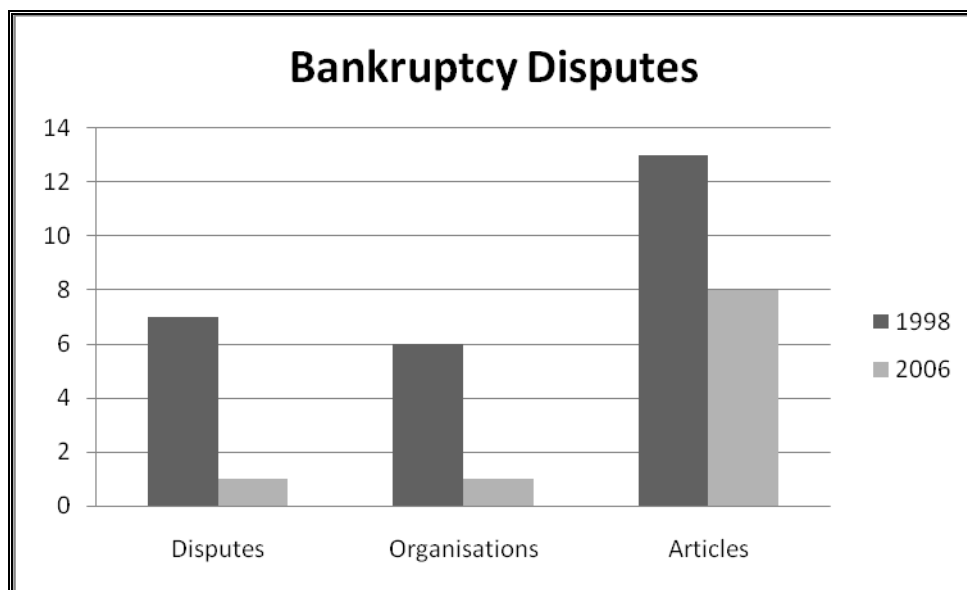
### 2.1 Second Order Codes (Management)

The discussion of the second order codes contains brief accounts of all relevant disputes. If a further clarification is required, readers can refer to a relevant template of the corresponding dispute contained in appendix 9a for 1998 and appendix 9b for 2006. In this section all accounts of the coded corporate disputes are presented in bullet points except for the last category, which due to its large size had to be summarised in a table.

#### 2.1.1 Bankruptcy

With regard to the newspaper coverage featuring bankruptcy proceedings, 7 disputes (6 different organisations) were identified in articles published in 1998 and only one dispute (1 organisation) in 2006. A total of 13 articles captured the 7 bankruptcy disputes in 1998, whereas the single case pertaining to 2006 was reported in 8 different articles (see graph 4.6). This suggests that the single bankruptcy dispute reported in 2006 had a disproportionately large impact on perception in comparison with individual cases reported in 1998.

Graph 4.6: *Bankruptcy Disputes*



Bankruptcy disputes reported in 1998 were almost exclusively connected with the unfulfilled financial obligations of affected organisations. They were as follows:

- Failure to meet outstanding debt obligations (Tatneft)<sup>47</sup>.
- Creditors were pushing for bankruptcy because the parent re-diverted cash flows away from its subsidiary (Sidanko).
- Unprofitable plant protected from bankruptcy because of the far-reaching social implication (Achinsk Alumina Combine).
- Bankruptcy of a bank that failed to pay its depositors after the financial crisis (ABS Agro).
- Two banks lost their operating licenses and were bankrupted after the financial crisis. The put option designed under the British law was not recognised by the Russian law (equal treatment of all shareholders) meaning that investors could not recover their money (EBRD).
- A company failed on debt repayment when a court sent marshals to seize its property on behalf of creditors. The government issued a presidential decree extending the credit (ORT).

There was one bankruptcy dispute apparently not directly connected to a commercial entity's inability to meet financial obligations:

- Bankruptcy proceedings were used in order to gain control of a subsidiary (Sidanko).

Three main themes emerge from the above. First, in 1998 bankruptcies affected unprofitable entities. These entities were unprofitable because they were mismanaged (Tatneft, Sidanko, Achinsk, ORT). Secondly, in addition to poor management, tough external conditions, at large caused by the uncertainty following the financial crisis, forced some companies into liquidation. The latter observation was particularly relevant to companies within the banking sector such as ASB Agro and EBRD (who had to write-off its investments into two smaller Russian banks). Finally, certain entities were protected from bankruptcy due to the far-reaching social implications that such proceedings would have caused. In the instance of Achinsk Alumina Combine, the government had no choice but to

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<sup>47</sup> The subsequent analysis of the third-order codes provides references to the corresponding second-order codes as well as relevant templates contained in appendices 9a and 9b.

protect the entity because it was the main employer in the region, despite it being systematically misappropriated by the management. Moreover, bankrupting such an entity as ORT (main television channel) would have reduced the government's grip on the crucial opinion polls. An entity, that by all accounts should have been comfortably profitable, suffered from a constant drain on its resources caused by the self-centred actions of influential stakeholders.

Bankruptcy proceedings can be an adequate response in the context of the above identified themes. In a capitalist setting, unprofitable entities should be liquidated and their assets sold to the highest bidder (Fox & Heller, 2000). Unfortunately, that was rarely the case in the 1998 environment in Russia. Much too often self-centred stakeholders (unusually management) prevented bankruptcies by manipulating the system. Nevertheless, it is important to acknowledge that the system, despite being perceived as weak and incompetent, often called for the right actions. In other words, those bankruptcies should have happened but in some instances did not because of the self-centred individuals (including the government officials) who had an immense capacity to manipulate the system of governance to their advantage.

In 2006 only one case of a bankruptcy was featured in the Moscow Times articles. As stated before, it was a much more influential (in terms of the impact it created on investor perception) case than any of the bankruptcies discussed with reference to the 1998 reporting because of the amount of coverage that this highly politicised case received.

In contrast to the previously discussed cases, the bankruptcy of Yukos was not brought about by the company's inability to settle its financial obligations, but by the government who systematically sought to destroy an economically viable entity. The government brought massive back-taxes claims against the company because, allegedly, its owner refused to reaffirm his loyalty to the Kremlin. It is entirely possible that the company and its owners were in fact guilty of ubiquitous tax evasion. However, it can be suggested with a reasonable degree of confidence that this is an example of a selective application of law because other Kremlin-friendly entities (allegedly just as guilty of similar violations) did not experience the same pressure from the authorities. In this regard, it is evident that contrary to the

1998 environment, the sole case of 2006 demonstrates a severe lack of integrity in the system, which nevertheless has accumulated an unchallenged capacity to regulate the environment.

#### 2.1.1.1 Implications for the Rule of Law with Reference to Bankruptcy Disputes

With regard to the perceived change in the rule of law, 1998 compares favourably with 2006 only on a single account. With regard to bankruptcy disputes reported in 1998, formal institutions (mostly courts) in the majority of reported cases proposed adequate rulings to bankrupt failing entities. In contrast to this, 2006 saw a corporate dispute where formal institutions (courts and tax authorities) were pressurised to produce rulings consistent with the government's agenda. The newspaper analysts suggested that this agenda was driven by self-centred actions of the Russian administrative elite.

However, in terms of perception, it is possible to conclude with a number of improvements with reference to the rule of law in 2006. Firstly, there were fewer reported instances of bankruptcies, despite the 2006 case being much larger in terms of coverage. Secondly, formal institutions appear to have much greater enforcement powers and the state has accumulated a greater capacity to exert influence over previously extremely powerful financial structures within the country.

Moreover, there were no reported instances when the government blocked bankruptcies of unviable entities. Finally, there were no reported instances when a bankruptcy was initiated by an interested private party in order to seize control.

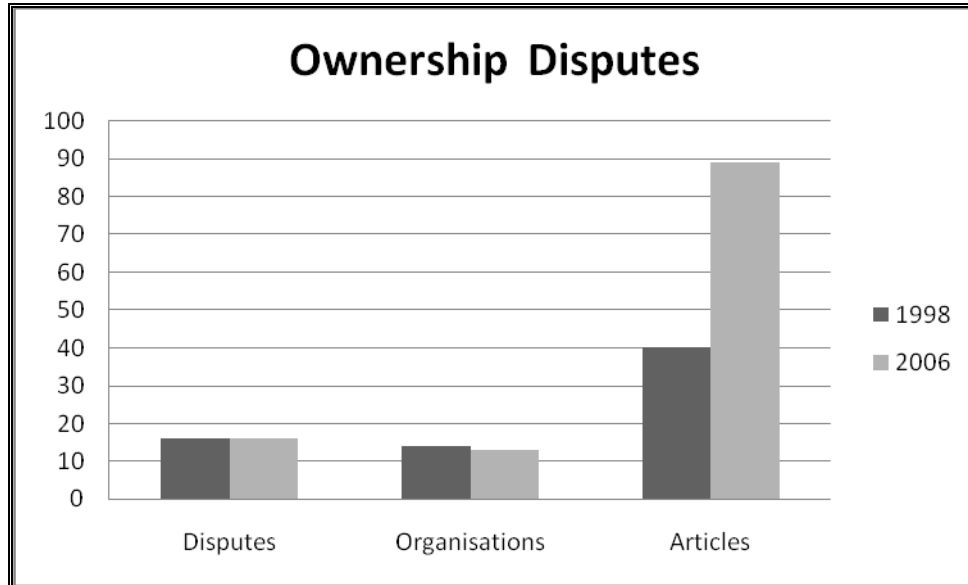
#### 2.1.2 Ownership

With reference to the Moscow Times coverage featuring ownership, 16 disputes (14 organisations) were identified from articles published in 1998 and 16 disputes (13 organisations) in 2006. A total of 40 articles captured the 16 ownership disputes published in 1998, whereas the 16 disputes in 2006 were reported in 89 different articles. In contrast to the previously discussed category, ownership



disputes in total received more coverage and therefore created a greater impact on perception in the more recent year. However, the nature of ownership disputes has evolved over the period under consideration.

Graph 4.7: *Ownership Disputes*



With regard to ownership disputes reported in 1998, three distinct themes emerged from the content of the analysed articles. These themes are ownership restrictions, contested ownership, and politically motivated re-allocation of property. The latter category is also applicable to ownership disputes pertaining to 2006. However a different theme termed ownership disclosure has been identified after a review of the content of 2006 ownership disputes. The themes and brief outline of relevant ownership disputes are presented hereunder.

#### 2.1.2.1 Politically Motivated Re-allocation of Property and Ownership Restrictions (1998)

- Gazprom’s managers set up a gauntlet of limitations to discourage outside shareholdings. Foreigners were barred from buying domestic stock and the company’s registrar refused to accept trades unless the shares had first been offered to Gazprom (Gazprom).
- \$1.5 billion loan from the World Bank was on condition that the government would reform Gazprom and the gas industry making it more open to new entrants (Gazprom).

- Cancellation of trust agreement under which the head of Gazprom also managed a 35% stake. The Federal Audit Chamber made this announcement as Vyakhirev (Gazprom CEO) fell out of favour with the government (Gazprom).
- The State Duma, parliament's lower house, passed a bill restricting foreign ownership in UES to 25% despite Yeltsin's apparent opposition. The issue was complicated by the fact that at the time foreigners had already bought around 30% of the company. The mechanism for buying back the 5% was unclear<sup>48</sup>. The bill was the result of political infighting between Yeltsin and communist dominated Duma, and was challenged in the courts (UES).
- A prominent foreign investor (Kenneth Dart) was investigated by the state Antitrust Committee which sought to establish whether he colluded with other shareholders to control more than 20% of Sibneft's subsidiary without the required permission from the committee. Dart had fallen out of favour with the government for his vocal criticism of the country's corporate governance environment (Sibneft).
- The results of high profile privatization deals (particularly with reference to Norilsk Nickel) were threatened with being reversed. The fact that Duma voted unanimously in favour of the reversal through the courts indicated a great deal of public dissatisfaction with the 'loans-for-shares' deals (Norilsk Nickel).
- The government decided to re-nationalise Vyborg Paper Mill and supported employees in their efforts to oust its new untrustworthy owners (Vyborg Paper Mill).

#### 2.1.2.2 Contested Ownership (1998)

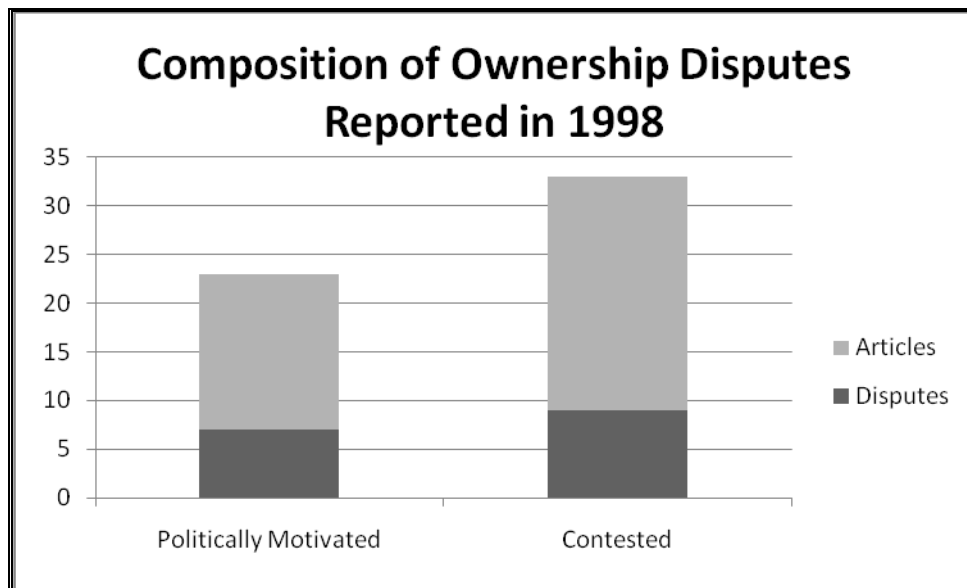
- Yuksi made a surprise announcement that it had no business relationship with Amoco which invested more than \$100m in the joint development of an oil field (Yukos).

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<sup>48</sup> The Russian Constitution explicitly forbids expropriation of property, and the state could not afford the \$600 million it would cost to buy back the 5 percent of foreign-owned stock.

- The company that was appointed to manage shares of Magnitogorsk resisted the handover of shares as collateral for the loan because the stake represented its main asset. Sharipov encouraged a number of transactions involving foreign partners and the local share registrar to hide the shares (Magnitogorsk).
- Those who attempted to hide the stakes in Lebedinsk Ore Mining Plant did so by selling it to a foreign company which no doubt was closely affiliated to Russian partners. The whole pursuit of shares by the government might have been caused by the pressure from the IMF that was calling for a greater effort to collect money on the part of the Russian government (Lebedinsky Ore Mining Plant).
- Sergiyenko, former CEO of Kubanksy Gips-Knauf, was suspended from office on allegations of theft, mismanagement and tax manipulation. His response was to hold his own meetings, remove Knauf from the company's name, and issue 64 percent of new shares to dilute the rightful owners' stake. 30 court decisions were ignored and the local authorities supported the coup arguing that the plant should be re-nationalised (Knauf).
- The State Anti Trust Committee's decision to allow the transfer of a stake to AssiDoman was declared illegal by the Moscow Arbitration Court. It was unclear why the legitimacy of AssiDoman's stake in Segezhabumprom Paper Mill was questioned. The only reasonable explanation would be an effort from either a minority shareholder or a third party to take control and ownership of the paper mill (AssiDoman).
- The Russian joint venture partner illegally ousted American partners (fast food chain Subway), renamed the entity to Minutka, and assumed control and ownership of the company (Subway).
- Managers of Lomonosov Porcelain Factory denied foreign investors access to the factory and its books on the grounds that the brokerages that sold the stakes had originally purchased them illegally (Lomonosov Porcelain Factory).
- Local authorities attempted to seize ownership (re-nationalise) of Kuznetsky Mine allegedly because the mine stood a good chance of returning to profitability following a major revamp by foreign investors (Kuznetsky Mine).
- A state owned company used its influence to negotiate a lease agreement in its favour depriving the foreign investor of any guarantees thus driving the foreign investor out of the project (MCCI).

Graph 4.8: *Composition of ownership disputes and the corresponding amount of coverage in 1998*



#### 2.1.2.3 Politically Observed Re-allocation of Property and Ownership Restrictions (2006)

- The government broke its promise to sell a 75% stake in Svyazinvest to strategic investors because it was looking for a politically acceptable partner (Svyazinvest).
- An agreement that a significant ownership stake in a joint venture with Gazprom would go to Moncrief was broken in favour of BASF who received much stronger political support (Gazprom).
- The government and Gazprom put pressure on foreign led projects using environmental non-compliance as a negotiating tool in order to secure favourable terms for Gazprom's (or Rosneft) entry (Gazprom).
- The government, possibly arbitrarily, imposed back-tax bills on Yukos in an effort to seize ownership of its main assets. The decision was linked to Khodorkovsky's support of political opposition. The case was disputed in local and international courts including the US court case when high profile government officials were 'legally served'. The government's onslaught was eventually legitimised by the international community when a British judge cleared the way for Rosneft's listing on the LSE. Rosneft ended up scooping up most of Yukos' assets in a number of highly non-transparent auctions (Yukos).

- The government used the Natural Resources Ministry and a number of mid-ranking officials in order to force Royal Dutch Shell to accept Gazprom's entry into Sakhalin Energy on favourable terms. Previously, the Russian government was angered by Shell when the company increased its cost estimate for the project. Under the Production Sharing Agreement (PSA)<sup>49</sup>, that meant that the government would have had to wait longer before it received any money from the project. Because of the new cost estimate and high price of oil and gas, the government decided to renegotiate the terms of the contract which admittedly were not in Russia's best interests (Royal Dutch Shell).
- The Russian government felt it was not in the interests of the country to allow foreign led projects (such as Total's Arctic Khoryaga oil field) to continue to operate under the original PSA terms. The decision was based on the fact that macro economic conditions i.e. sharp increases in oil prices rendered the PSA agreements highly unprofitable for the Russian side. The decision to re-establish the ownership structure came from the government and was contrary to the agreements and promises made in the past (Total).
- The Russian government used its usual tactics of bullying companies into compliance (surrender some licenses and stop competitive bidding) by bringing allegations against oil majors. In the instance of LUKoil it was the Natural Resources Ministry's environmental regulator that blamed LUKoil for environmental violations and development delays (LUKoil).
- The government used environmental violations and non-compliance with the license agreement to force TNK-BP to accept 'Gazprom tailored' terms of restructuring (TNK-BP).
- Derepaska and Vekselberg were planning to merge their aluminium assets together after years of bitter rivalry. The chances of the merger going ahead were predicted to be higher if the oligarchs offered a stake to the state (RusAl).

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<sup>49</sup> Production Sharing Agreements were designed in the 1990s with the aim of attracting and protecting foreign investors by offering tax breaks and nominating a foreign court to settle disputes.

#### 2.1.2.4 Disputes Related to Disclosure and Transparency of Ownership (2006)

- The Zurich arbitration tribunal ruled that the IT and Communications Minister, Leonid Reiman, was the ultimate beneficiary of the IPOC fund. The minister (who denied his connection with the fund) diluted the state's interest in MegaFon using his powers as the IT and Communications Minister (MegaFon).
- Trading in preferred shares was cancelled because of an ongoing investigation into alleged abuses by former managers. The prosecutor general's office asked a number of brokerages to disclose the beneficiaries of Transneft. The most interesting point however was the fact that disclosing beneficiaries was predicted to worsen the sentiment on the stock market because of the constantly questioned legitimacy of privatisation (Transneft).
- The US authorities wished to scrutinize links between Abramovich and the Russian Government<sup>50</sup> in relation to Evraz's bid for Oregon Steel (Evraz).
- Gazprom cut gas supplies to Ukraine breaking existing contracts and agreements. The company used its monopoly power to renegotiate better terms. In the instance of the agreement with Ukraine, a company with an undisclosed ownership structure (Rosukrenergo) was nominated as a trader. As a result of that, billions of dollars went unaccounted for (Gazprom).
- RusAl disclosed its ultimate beneficiary<sup>51</sup> because of a condition for a loan received from the EBRD (the European Bank for Reconstruction and Development). This in turn triggered a suit from a former business partner which had an impact on investor confidence (RusAl).
- The chairman of Novolipetsk sold the company supplying raw materials that he owned to the group in order to address concerns over transfer pricing from the shareholders (Novolipetsk).

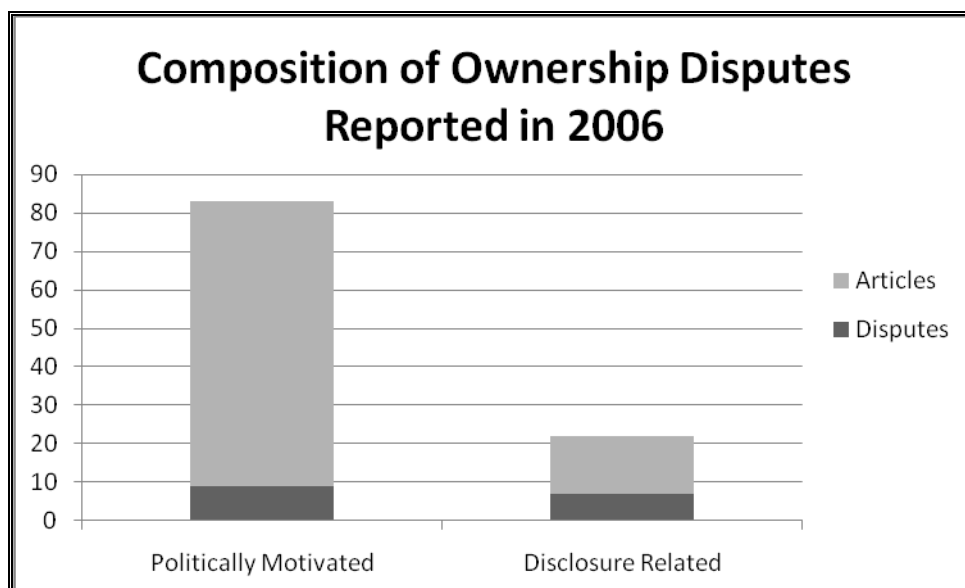
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<sup>50</sup> Because the relationship between business and politics is so intertwined in Russia, the American authorities could use the investigation of that relationship as a tool to block the bid on political grounds. Equally so, the American authorities need to know what motivated the actions of the investor.

<sup>51</sup> EBRD and felt it was necessary for RusAl to disclose its ownership structure. It turned out that Derepaska was the sole shareholder of the group. This disclosure led to a former partner's legal complaint because he felt his debt had not been settled. He sued the company for \$3b in compensation. With regard to other former partners, out of court settlements had been struck.

- Mordoshov (CEO of Severstal Group) sold the company (that he owned) supplying raw materials to the group in order to address concerns about the group's transparency. Previously, these types of assets were acquired by Kremlin insiders involving a series of transfer pricing schemes (Severstal).

Graph 4.9: *Composition of ownership disputes and corresponding amount of coverage in 2006*



The above comparison shows that politically motivated re-allocation of property and ownership restrictions category became a much more prominent feature of the perceived environment in 2006. With regard to this subtheme of ownership disputes, not only did the number of reported instances rise from 7 to 9, but more significantly, the number of articles covering this type of ownership disputes increased from 16 in 1998 to 74 in 2006. In 1998 there were only two disputes of this nature reported in more than two separate articles: a dispute involving re-nationalisation of the Vyborg Paper Mill (3 articles) and an imposition of foreign ownership restriction below existing level in UES (8 articles). However, in terms of the impact on investor perception and with reference to 2006 these disputes are no match for a highly contentious re-nationalisation of Yukos (23 article), Shell's fight over Sakhalin 2 project (25 articles), and TNK – BP's troubles over Kovykta gas field (15 articles). In 2006 these disputes contributed a great deal to forming a perception of how the Russian government handles high profile corporate affairs involving conflicts of interests. The key issue here is arbitrary application of law. Very importantly, the example of this practice set by the Russian government is

replicated on a smaller scale in the form of ubiquitous corporate raids. These corporate raids are possible because of the involvement of corrupt governmental agencies such as tax authorities and health and safety inspectorates.

The category of contested ownership ceased to be a relevant feature of reported material in 2006. This subtheme was visibly present in 1998 reporting (9 disputes covered across 24 articles) with a number of prominent disputes such as contested ownership of Subway – Minutka (7 articles), challenged legitimacy of AssiDoman’s ownership stake in Segezhabumprom Paper Mill (6 articles) and Magnitogorsk management’s illegal refusal to hand over an ownership stake they had been entrusted to manage (3 articles). Disputes of this nature are typical of an early stage transition which is normally associated with weak property rights. In contrast, 2006 reports illuminated no instances of such conflicts<sup>52</sup>. Instead a new subtheme related to disclosure and transparency of ownership (7 disputes covered across 15 articles) emerged. A number of companies were pressed to disclose their ultimate beneficiaries causing concern among certain stakeholders when ownership was disclosed voluntarily (Evraz, RusAl, Novolipetsk, Severstal) and when it was not (Megafon, Gazprom, Transneft).

#### 2.1.2.5 Implications for the Rule of Law with Reference to Ownership Disputes

With regard to ownership disputes, there is no evident change in perception towards a greater rule of law in the country. If anything, extensive coverage of politically motivated corporate disputes has caused a deterioration in the perceived environment by firmly setting the image of legal nihilism (i.e. the belief that all established authority is corrupt) in the eyes of foreign investors. This perception is more detrimental to Russia’s corporate image now than it was in the 1990s because earlier it was attributed to an inevitable side effect of transition, whereas now it is seen as a more permanent, deeply rooted feature of the environment. Prevalence of this aspect, coupled with a much greater capacity of the state,

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<sup>52</sup> A conclusion that such disputes do not happen anymore cannot be drawn from this data. However, it can be stated that disputes of this nature have become less of a characteristic of foreign investor perception of the environment.



represents a bigger threat to previously powerful foreign investors and hence produced more negative coverage in the pro-western press.

On the positive side, in 2006 a change in perception towards stronger property rights (outside previously discussed situations when there is direct involvement by the government) manifested itself through the absence of coverage of contested ownership disputes. In the late 1990s businesses were frequently forced to give up their property when a stakeholder with stronger 'physical presence' could affectively deny access to rightful owners for no apparent reason (Knauf, Subway). In 2006 disputes falling into this subtheme were not reported. Such a crude redistribution of property ceased to be a prominent feature of the perceived environment. Similar to previous conclusions however, a degree of caution must be expressed with regard to the latter proposition. The data gathered by the author does not suggest that crude redistribution of property does not take place in contemporary Russia. Conversely, anecdotal evidence suggests that it does take place in the form of outrageous corporate raids. However, such raids require the involvement of governmental agencies and therefore serve as an explanation for increased reported activity with regard to the subtheme which is called the politically observed redistribution of property. Nevertheless, from the western perspective an absence of coverage directly related to the contested ownership subtheme must have had a positive impact on investor perception of the business climate in the country.

Secondly, with regard to the increased presence of the disclosure subtheme, the fact that major owners started (were forced) to disclose their shareholdings serves as a sign of an increased confidence in public acceptance of the de facto ownership structures in the country. Although such disclosures proved to be a painful process filled with subsequent litigation (e.g. the case involving aluminium producer RusAl), it is nevertheless a step in the direction of a greater legitimacy of existing ownership structures. Such formal disclosures were impossible in the 1990s due to an unpredictable public reaction to the newly established owners after the extremely unpopular loans-for-shares deals<sup>53</sup>.

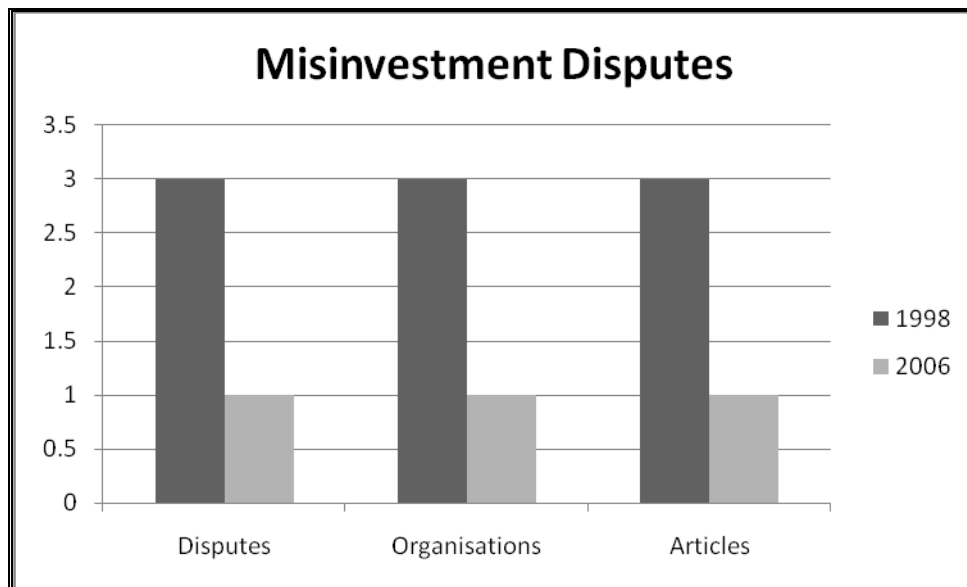
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<sup>53</sup> Loans-for-shares was a privatisation scheme whereby the government sought to raise much needed finance by offering highly discounted shares in most valuable Russian companies as collateral for loans.

### 2.1.3 Misinvestment

With regard to disputes arising as a result of misinvestment, 3 instances affecting 3 organisations were reported in 3 articles in 1998. In 2006 a single instance was reported and only in one article. This is the smallest category but is nevertheless included in the analysis because it reveals non financial motives behind high-profile business decisions. Even though the data is extremely scarce in relation to reported instances of misinvestment, a conclusion in favour of 2006 can still be drawn from the numbers presented in graph 4.10.

Graph 4.10: *Misinvestment Disputes*



In 1998, all reported instances of misinvestment were externally imposed. Here, the role of government in explaining the non-financial motives of business decisions is rather explicit. A brief outline of the three cases of disputes reported in 1998 is presented hereafter:

- Gazprom's decisions to purchase Inkombank and a media outlet were motivated out of pre-election oligarchic manoeuvring rather than prudent business acumen (Gazprom).

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Kremlin insiders provided the money knowing that the government would default on repayments giving them rights over much sought after collateral.

- Achinsk Alumina Combine was protected from bankruptcy because the local administration was trying to prevent the plant's collapse due to far-reaching social implications (Achinsk Alumina Combine).
- Political connections led to bailing out of some banks such as SBS Agro and not others. The decisions were not linked to operational efficiency of banks in question (SBS Agro).

In 2006 there was only one reported instance when an investment was not in the financial interests of one of the major shareholders involved:

- Both shareholders of VimpelCom had a blocking stake. One of them was interested in VimpelCom purchasing a competitor of the other shareholder. The Russian shareholder provided misleading information at the disputed extra-ordinary shareholders meeting and got the vote its way (i.e. in favour of the purchase). Telenor disputed the decision in the Russian courts and threatened to take the case to an American court (VimpelCom).

#### 2.1.3.1 Implications for the Rule of Law with Reference to Misinvestment Disputes

It is evident from the purely inductive comparison presented above that the biggest difference between the two time periods is a perceived move away from situations when businesses were forced to misinvest by the external environment to a healthier situation when some of the key investment decisions are internally challenged by affected shareholders and stakeholders. In 1998 the chaotic post-privatisation environment dictated the terms. Often firms (particularly larger ones) had to engage in projects that did not make economic sense to profit-oriented shareholders. Gazprom's involvement in a media outlet and opposition to a socially damaging bankruptcy of Achinsk are examples of misinvestment reported in 1998. Conversely, the single case reported in 2006 can be seen as a purely internal affair where shareholders encountered a conflict of interests arising as a result of a possibly viable investment project<sup>54</sup>.

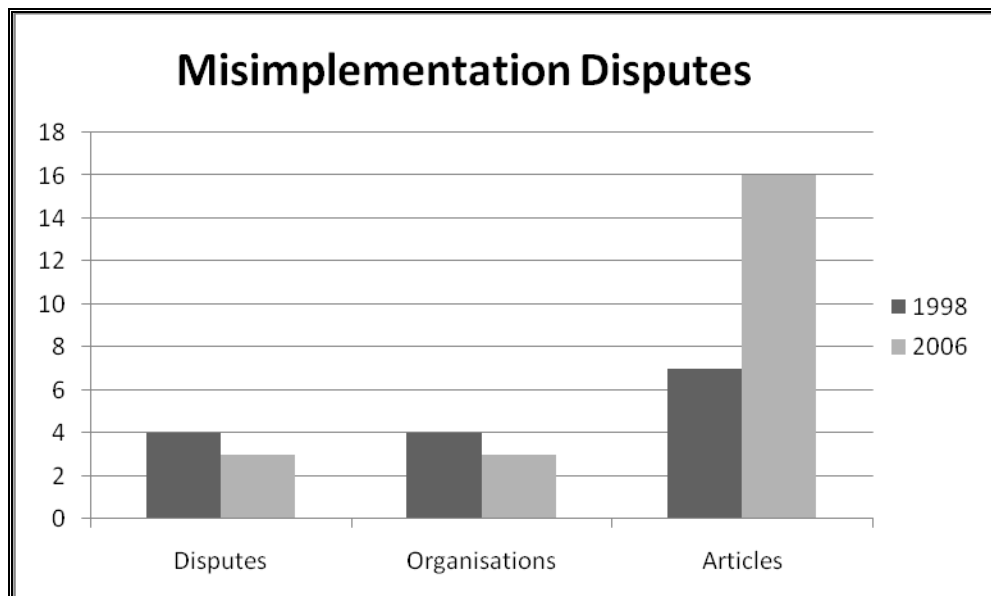
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<sup>54</sup> The way a major shareholder dealt with the situation was by no means a demonstration of good corporate governance practice and will be analysed in more detail in the dispute resolution section.

### 2.1.4 Misimplementation

Similar to misinvestment, misimplementation is a small category in terms of the number of separate disputes covered by the newspaper. There were 4 instances of this dispute affecting 4 organisations in 1998 versus 3 cases (3 organisations) reported in 2006. However, these disputes had a much larger impact than misinvestment disputes because of the amount of coverage received (see graph 4.11). Clearly, 2006 stands out in this regard suggesting that failure to implement viable investment projects was a prominent feature in forming investment perception in the latter year of the investigation.

Graph 4.11: *Misimplementation Disputes*



In 1998 there were a variety of reasons behind the failure to implement viable investment projects. Among such reasons were political differences between key individuals seeking to form a joint venture, failure to negotiate mutually acceptable terms of partnership and value destroying actions by a partner. Examples of such corporate conflicts reported in 1998 are further detailed below:

- A joint venture between Sibneft and Yukos (Yuksi) was postponed and eventually terminated because of political differences among top management (namely Berezovsky who was politically active and Khodorkovsky who preferred to keep a low political profile) (Yukos).

- Tax and wage arrears, fight for control and ownership at Vyborg Paper resulted in a failure to implement what otherwise would have been a viable project. The property was eventually re-nationalized (Vyborg Paper Mill).
- Most-Bank alleged serious abuses on the part of Uneximbank calling for government regulators to investigate the matter. Uneximbank, however, argued that the operations of United Card Service (joint venture) had been audited by Price Waterhouse who did not uncover anything suspicious. Most-Bank pulled out of the venture citing unwillingness to accept responsibility for the gross misconduct on the part of the joint venture partner (Most Bank).
- Many questioned legitimacy of Prosystem GmbH's stake in Kuznetsky Mine even though the actual sale had taken place. There were efforts to reverse privatisation. Those were probably linked to the fact that the mine stood a good chance of returning to profitability after a major revamp by the foreign investor. It is possible that the local administration and other parties were interested in gaining control over the mine and used the political context as a pretext for their self-centred actions. The foreign investor failed to find a compromise with the local stakeholders (Kuznetsky Mine).

In 2006 two cases of corporate disputes were arguably caused by a failure to reach a compromise with powerful stakeholders who eventually intervened with the goal of redistributing the property. The third case of a failed merger bid was evidently caused by a lack of managerial competence. Key aspects of these disputes pertaining to 2006 are presented below:

- In a conflict with Shell, the Russian government made full use of the Natural Resources Ministry and its powers to revoke licenses. In general it is extremely difficult not to violate environmental rules in the process of oil and gas extraction, particularly if you are forced to use local subcontractors which one has little control over. Clearly, based on a technicality in the point of law, the Russian government had the right to revoke licenses and some violations probably did take place (this made it possible for the government to attack the Production Sharing Agreement<sup>55</sup> which offered a great deal of protection to foreign partners). Additionally, Shell annoyed the government by increasing the costs of the project. This meant a longer wait for the government before it was to get any returns from the agreement (Shell).

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<sup>55</sup> Production Sharing Agreements were designed in the 1990s to protect major investors from the unstable legislative environment in Russia. As a rule, such agreements nominated a foreign court (usually Stockholm Arbitration Court) as an arbitrator.

- The European shareholders did not welcome Mordoshov's (Severstal) bid because they suspected foul play on the part of the unknown Russian businessman. Also, it was very easy for the competitors for Arcelor's assets (Mittal) to play the corruption card, i.e. a rich Russian who was not doing a great deal to introduce himself to shareholders, was a bit of a dark horse, and therefore was very likely to be/have been connected to the criminal underworld (Severstal).
- A well-connected local business group used fire violation (this aspect of Russian legislation is very vague) to put IKEA at a disadvantage ahead of a busy trading period. It was also very possible that the business group had more fundamental plans to do with the permanent closure of the mall. In these circumstances, based on the previous experience where the company invested in the infrastructure, IKEA had no choice but to negotiate a common solution with the stakeholders involved. The courts here were clearly used as an instrument at the disposal of the influential local parties. Had IKEA maintained good relationships with the power structures in the region, the assault would probably not have taken place (IKEA).

#### 2.1.4.1 Implications for the Rule of Law with Reference to Misimplementation Disputes

Despite the fact that the number of corporate disputes within this category fell by one instance, increased coverage in 2006 has had a negative impact on the perception of how easy it is to implement viable investment projects in Russia<sup>56</sup>. A more advanced stage of Russia's transition has not led to a more balanced relationship with key stakeholders. This situation was probably caused by a conflict of interests arising as a consequence of highly discounted sales of the past<sup>57</sup>. Under new economic conditions these discounted sales became politically prohibitive and a failure to renegotiate claims has led to the government-assisted redistribution of property. From an optimistic view point this could be interpreted as a fix in the very foundation of the Russian corporate environment, nevertheless, on the surface investor perception has suffered a great deal from the well-published examples of crude interference in the business processes.

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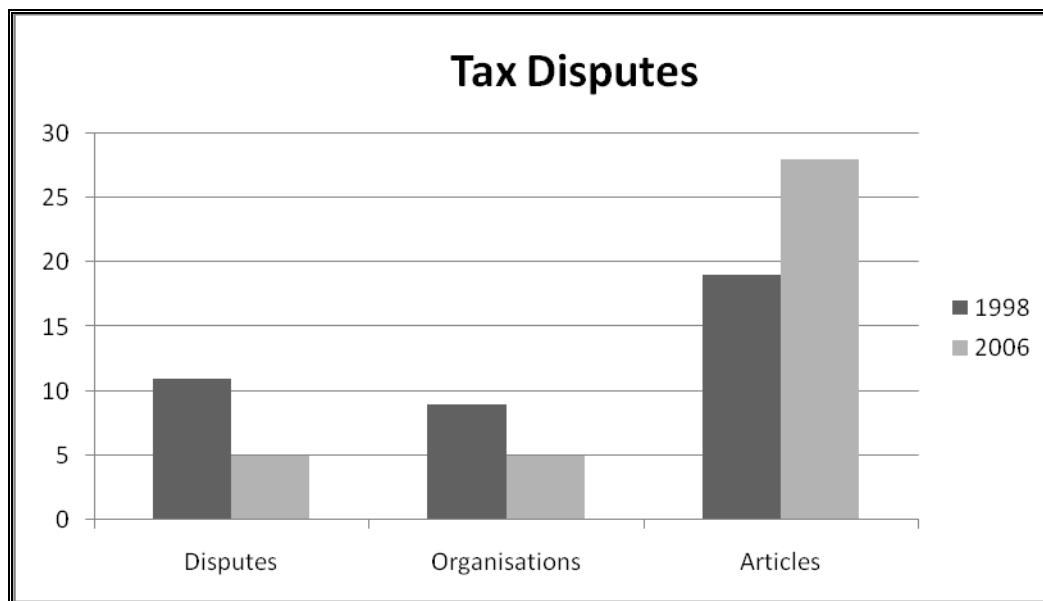
<sup>56</sup> Actions of influential stakeholders will be considered in more detail in the subsequent sections dedicated to the analysis of enforcement strategies.

<sup>57</sup> The period in question started when Russia began its transition from command to market economy.

### 2.1.5 Taxes

Corporate disputes involving non-payment of taxes occur frequently in the Russian business environment. The number of such disputes reported in 1998 was substantially higher than in 2006. However, similar to ownership and misimplementation disputes, the amount of newspaper coverage of these disputes increased noticeably in the more recent year of the investigation (see graph 4.12).

Graph 4.12: *Tax Disputes*



In 1998 instances of corporate disputes connected with non-payment of taxes were determined by two factors. The first factor related to a massive budget deficit that the government had to close by means of a very aggressive tax-collection policy (which did not spare even strategically important joint ventures and partnerships). Reported conflicts arising as a result of such practice suggest that the government was keen to impose additional tax liability on cash rich firms. The second factor was a product of a malfunctioning system where tax authorities were used as an instrument for diverting claims, assets and competitiveness from less protected (connected) corporate entities. Further details of such disputes pertaining to 1998 are presented hereunder:

- Russia's dependence on International Monetary Fund forced authorities to scale back on the tax breaks promised by the presidential decree to the Gaz – Fiat joint venture (Gaz).
- The Russian tax police specifically targeted the KIA venture in Kaliningrad. The seizure of assets was not authorised by the courts and it was suggested that the tax authorities were in cahoots with the local used-cars importers who tried to disadvantage their direct competition (KIA).
- The Russian tax police seized assets of two Gazprom subsidiaries. This was an order by the new taxation chief, Boris Fyodorov who was charged with the task of improving tax collection rates. The bank accounts and property of Orenburggazprom and Uraltransgaz were ordered to be seized<sup>58</sup> (Gazprom).
- The local authorities enlisted the services of the unions to enhance their negotiating power with Yukos officials over disputed taxes. It was unclear whether the claimed tax arrears actually existed. The local administration together with union representatives tried to get more money out of Yukos; it is possible that the motive was to represent the interests of the population and ordinary workers of the company, but in the environment of 1998 a more pragmatic interpretation would suggest indirect expropriation of shareholder wealth (Yukos).
- Tomskneft, a subsidiary of Yukos, was facing bankruptcy because it owed 400 million rubles (\$21 million) in taxes to the federal budget and another 200 million rubles to the local budget and the pension fund. It also owed 300 million rubles to its staff in back wages. A Yukos spokesman said that the court that ruled in favour of bankruptcy had ignored a proposal from Yukos to cover its subsidiary's debt without giving reasons (Yukos).
- The city of Omsk saw its regionally gathered tax revenues fall from 65 percent of its budget to only 38 percent. Omsk Mayor Valery Roshchupkin responded by raising local taxes - adopting a 2 percent city tax on turnover (not profits) that prompted 30 of the Omsk's largest businesses, including many with ties to the governor, to reregister "offshore," just outside the city limits. When Sibneft was re-registered outside the city, the Omsk mayor's office introduced a 35-ruble-per-ton tax on crude oil processed by the refinery, a tax Sibneft contested in court (Sibneft).

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<sup>58</sup> The State Duma protested loudly claiming that the action would cause a threat to national security.



- With reference to Sidanko, the government came up with a resolution whereby oil companies were denied export quotas if they fell behind on tax repayment terms (Sidanko).
- Irkutsk's regional administration sought to take control over a refinery (Sidanko's subsidiary) on the back of tax allegations by installing external managers further to a ruling made by the regional arbitration court. Sidanko responded by stopping deliveries of crude oil to the refinery. It had been suggested that the motive behind the proceedings was of a political nature, i.e. preserving jobs and enterprise in the region. The task was not of a commercial character because otherwise the entity would have been declared bankrupt as it was seen as unprofitable without the Production Sharing Agreement which the government was unwilling to grant (Sidanko).
- The government had to boost tax collection in order to close a substantial budget deficit. In this particular case the decision was made to recover some of the tax debt through a bankruptcy of Norilsk Nickel's subsidiary. The company appealed the decision in an arbitration court arguing that the tax debt of \$40m was calculated incorrectly (Norilsk Nickel).
- An unidentified party was using tax authorities to exert pressure on Knauf to either surrender control, or simply share profits. The arbitration court ruled in favour of the decision made by the tax authorities<sup>59</sup> (Knauf).
- AssiDoman was charged with back taxes pertaining to the paper mill they had purchased. The fact that a solution to the tax and bankruptcy issues depended on the heads of the respective agencies<sup>60</sup>, and not an objective criteria suggests a very arbitrary approach. Also, pledges made by the president were not an indication of what was right or wrong, but simply populist exclamations during foreign visits. Meanwhile the state bankruptcy and tax authorities froze the accounts preventing the company from investing in capital improvements (AssiDoman).

In 2006 reported tax disputes were almost exclusively connected with the government's drive to re-establish control over strategically important assets. These disputes (although fewer in number in comparison with 1998 data)

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<sup>59</sup> Although the tax police were formally right as Knauf made an accounting mistake, the former refused to consider the evidence (receipts) supplied by Knauf.

<sup>60</sup> The company sought to establish personal relationships with key individuals in the position of power such as Chubais and Mostovoi. Their efforts were cancelled out by the reshuffle.

generated a large amount of press coverage and in that sense had a significant impact on investor perception of the deterioration of the rule of law in the country. In 2006 manifestation of the latter point took the form of arbitrarily imposed tax charges. Further details of reported tax disputes pertaining to 2006 are presented hereunder:

- The Russian Court system bounced criminal charges against AvtoVaz from court to court, but eventually returned all of the cases to the prosecutor's office which decided to cancel the investigation into the alleged non-payment of \$8m in back taxes. No explanation was given as to why the investigation had been closed. However, analysts suggested that the government was seeking to re-establish control over the car manufacturer by opening and closing criminal investigations and bringing in a symbolic suit against the joint-venture partner (General Motors) (AvtoVaz).
- The government detained Barinov (Nenets Governor) on suspicion of fraud and embezzlement allegedly after/because he complained against Rosneft's subsidiary which failed to pay taxes to the local budget and broke ecological standards. Rosneft claimed that the company was acting in accordance with all signed agreements and had nothing to do with the detention of the governor (Rosneft).
- The Russian government charged Yukos with a massive back-taxes bill in an effort to seize control over the viable company's assets. The decision was also linked to Khodorkovsky's support of political opposition and had very little to do with the way the company was managed (Yukos).
- TNK-BP learnt from the Yukos experience and did not challenge an imposed back taxes claim too aggressively in the Russian courts. The fact that the company did pay the questionable back-tax has been viewed as a relationship building opportunity with the Russian government and key stakeholders of the company (TNK-BP).
- The Audit Chamber felt it was wrong for Evraz to use off shore traders in order to minimize taxes. The Chamber ruled against the company (Evraz).

### 2.1.5.1 Implications for the Rule of Law with Reference to Tax Disputes

From analysing cases of tax disputes reported in the two years of the study, both positive and negative trends with regard to the perceived change in the rule of law can be revealed.

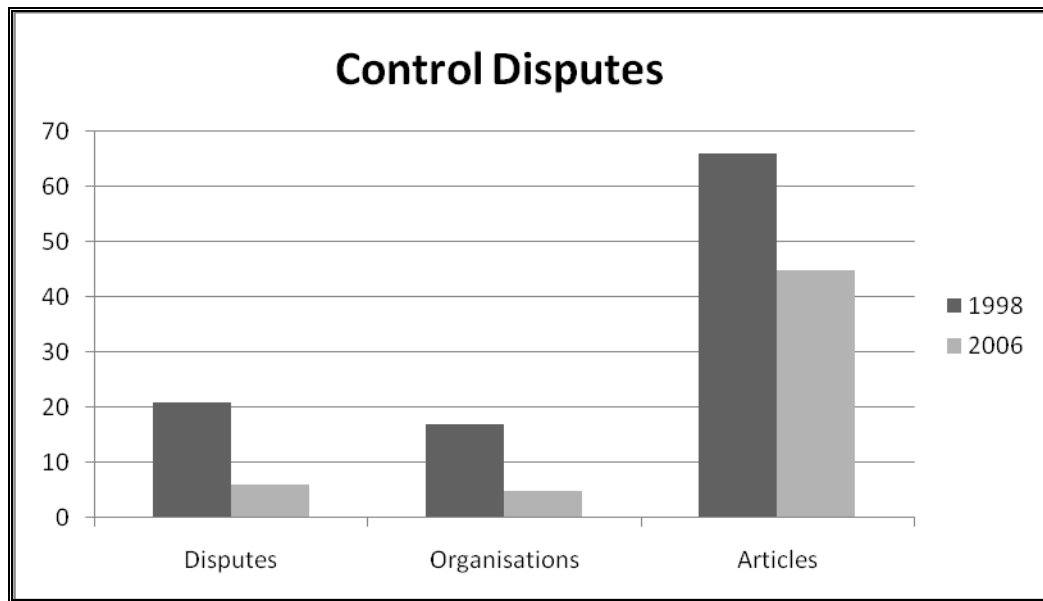
On the positive side, the Russian government does not need to resort to 'fire-fighting' measures of tax collection in order to close a loophole in its budget. In 2006 there were no reported instances when a cash-rich firm was compelled by the tax authorities to 'donate' its resources to the federal tax fund. Conversely, in 1998 there were 6 examples of such practice (Gazprom, Fiat-Gaz, Yukos, Sibneft, Sidanko, Norilsk Nickel). Secondly, instances when tax authorities acted on behalf of a private group of individuals in order to target a specific venture were not reported in 2006. Therefore, as far as investor perception is concerned there has been a positive change within the environment which is seen as more protected from the crude abuses of the tax system. In 2006 there were no equivalent disputes to what happened to Knauf, KIA and AssiDoman in 1998 when tax authorities acted as a tool for self-centred private stakeholders.

Nevertheless, 2006 was dominated by situations when the government used the tax system to achieve its political and economic goals. Examples involving AvtoVaz, Yukos and TNK-BP expose the arbitrary nature of this interaction. The tax dispute involving Rosneft also shows that the government is prepared to resort to the use of other formal institutions such as the courts in order to punish those who do not act in accordance with its de facto agenda. In 2006 it was these disputes that received a great deal of the newspaper coverage and hence considerably influenced investor perception of the rule of law in the country.

### 2.1.6 Control

With reference to control disputes, 1998 was a particularly eventful year with 21 disputes involving 17 organisations featured in 66 articles. This compares with only 6 disputes involving 5 organisations in 2006. Although similar to previous categories there was a lot more coverage per dispute in 2006, in total more was written about 1998 conflicts (see graph 4.13).

Graph 4.13: *Control Disputes*



The year 1998 was characterised by weak property rights and a poor corporate culture. In terms of disputes falling into this category, this means that there was a visible disparity between the level of ownership and a corresponding level of real control. According to the analysed disputes, such disparity occurred when:

- There were instances of corporate insubordination (Tyumen, Knauf, Kosmos TV, Subway).
- Outside groups exerted pressure on decision makers within their respective organisations (VimpelCom, Krasnoyarsk Hydro Plant, Knauf, MCCI).
- The board of directors accumulated a disproportionately large amount of control (Rosneft).
- Shareholders/creditors failed to get a fair board representation (Sidanko, Novolipetsk, Achinsk Alumina Combine, Inkombank).
- The nomination/dismissal process failed (UES, Electrosila, MFK Renaissance, Kosmos TV).
- Ownership was diluted ahead of voting on key issues (Yukos, Krasnoyarsk Hydro Plant, Subway).

- Aggressive takeover and bankruptcy proceedings were instigated against targeted organisations (Sibneft).

Further details of such conflicts are presented hereunder:

- Alongside booming growth came death threats and physical assaults on VimpelCom's employees. It was thought that the local criminal community had been trying to take control of the company (VimpelCom).
- Rosneft pushed through an amendment to the company's charter whereby the board of directors of Purneftegaz was given the authority to conduct transactions with up to 50 percent of the company's assets. As a result, the directors could effectively sell off the company's equipment, oil wells, transportation machinery, and so on (Rosneft).
- Menatep defaulted on a loan repayment. According to a previously signed agreement, 30% of Yukos' shares went to the bank as collateral, but Menatep's (Yukos) management decided to dilute the transferred stake through a share issue and by doing so reduced the leverage of the disgruntled bank (Yukos).
- The Omsk Oil Refinery was a profitable business. It became a takeover target when Sibneft was being formed. The refinery was merged with Noyabrneftegaz. The move was opposed by the General Director of the refinery Ivan Litskevich but he died as the battle was heating up. The merged company was privatised for a song under the loans for shares programme. Berezovsky benefited from the deal (Sibneft).
- The Irkutsk regional administration sought to take control over a refinery (Sidanko's subsidiary) on the back of tax allegations by installing external managers after a ruling made by the regional arbitration court. Sidanko responded by stopping deliveries of crude oil to the subsidiary (Sidanko).
- Bankruptcy proceedings were used in order to gain control of Chernogorneft (Sidanko's subsidiary). It was unclear why two creditors were left out of the bankruptcy proceedings. It is entirely possible that a behind the scenes agreement had been formed as the two creditors did not react to the news (Sidnako).

- The renegade director used support of the workers' collective of Tyumen's subsidiary in order to maintain his control. Paly gained support among fellow employees because he suggested that privatisation of Nizhnevartovsk was rigged in Alfa's favour (possibly not without considerable support from high-ranking officials like Chubais). Eventually, he (Paly) gave up or was bought out by the Financial Industrial Groups i.e. Alfa and Renova, because the parent (Tyumen) and the subsidiary (Nizhnevartovskneftegaz) were losing money (Tyumen).
- The Tanako FIG exerted pressure on the management of Krasnoyarskenergo to sell the stake in Krasnoyarsk Hydro Plant cheaply. Boris Nemtsov (Deputy Prime Minister) denounced the deal giving a clear indication as to the government's stance on the issue. The director of Krasnoyarskenergo was sacked. UES (the parent of Krasnoyarskenergo) proceeded with a legal challenge that failed to produce any results. Meanwhile Krasnoyarsk Hydro Plant issued shares to dilute the holding of the parent making it more difficult for UES to regain control. Krasnoyarsk Hydro approved the total of 30 percent dilution, but attracted attention from the Federal Securities Commission (Krasnoyarsk Hydro Plant).
- Two political clans, one headed by Deputy Prime Minister Nemtsov, the other by Prime Minister Chernomirdin were fighting for control of UES. Each wanted to appoint their men in the position of power (Brevnov and Dykov respectively). The fight was accompanied by accusations of corruption and bad management practice. The conflict however erupted when Dyakov called a meeting of the board of directors that voted to fire Brevnov, a 29-year-old former banker from Nizhny Novgorod brought in by First Deputy Prime Minister Boris Nemtsov to clean up the company's finances (UES).
- Chubais received the top job at UES as a trade off for leaving the government. The name of the famous reformer was tarnished by accusations of corruption. Nevertheless he was still the preferred candidate from the perspective of foreign investors for his reputation as a liberal reformer (UES).
- The majority shareholder of Electrosila decided that the existing director at the time was no longer suitable for them. It was speculated that the director needed to be replaced with someone who would be more active at recovering a lost stake on behalf of the shareholder. Siemens (the minority, but significant shareholder) protested saying that they were happy with the existing director who returned Elektrosila to profitability (Electrosila).

- Despite holding 40 percent of Novolipetsk's ordinary shares, a group of investors was blocked from getting board representation. The old management clearly did not want to share power with new shareholders, some of whom appeared as a result of the controversial loans-for-shares deals (Novolipetsk).
- The financial groups behind the new shareholders of Novolipetsk squeezed Trans-World out by means of blocking its vote. Such interest in Novolipetsk arose as a result of rosy forecasts for the industry. Also the investigation by the State Duma securities commission of the Trans-World Director must have been a coordinated effort (rather than a coincidence) in driving the British company away from the dominant position in the industry (Novolipetsk).
- A creditor (Alfa Group) of Achinsk Alumina Combine was pressing for the appointment of their own external manager and eventually bankruptcy of the combine. KRAZ, a FIG behind management existing at the time resisted the move. A local court ruled in favour of KRAZ (which was backed by local administration) extending its managerial capacity for a year (Achinsk Alumina Combine).
- Sergiyenko, director of Kubanksy Gips-Knauf, was suspended from office on allegations of theft, mismanagement and tax manipulation. His response was to hold his own meetings, remove Knauf from the company's name, and issue 64 percent new shares to dilute the Germans' (rightful owners) stake (Knauf).
- An unidentified party was using tax authorities to exert pressure on Knauf to either surrender control and/or simply share profits. The arbitration courts ruled in favour of the decision made by the tax authorities (Knauf).
- A candidate (Boris Jordan) was refused the position of CEO at MFK Renaissance on the technicality in the law, did not qualify in the context of that particular circumstance. Allowing a foreigner to be in charge of an investment vehicle could have made the Russian government vulnerable (MFK Renaissance).
- Uneximbank-MFK prevented representatives from Inkombank from voting on dismantling the board due to an alleged error on the part of the board. Inkombank's representatives did not receive ballots for the vote. Inkombank successfully petitioned the St. Petersburg Arbitration Court for an injunction on the meeting (Inkombank).

- A renegade director (Lapshin) at Kosmos TV took its shareholders to court over his dismissal. The court ruled in favour of the renegade director because it relied on the Labour code, rather than the Joint Stock Company Law, which is a higher order law that would have protected the shareholders more adequately (Kosmos TV).
- The Russian joint-venture partner illegally ousted American partners (Subway), renamed the entity to Minutka, and assumed control and ownership of the company. The case was taken to the Stockholm International Arbitration Court which ruled in favour of the American partners (Subway).
- A state-owned company, GlavUpDK, used its powers to negotiate the lease agreement in its favour depriving the foreign investor (MCCI) of any guarantees thus driving the foreign investor out of the project. The foreign partner turned to international courts that ruled in its favour (MCCI).

In 2006 all reported disputes pertaining to the control category directly involved the Russian government. In order to maximise its influence over major commercial and strategic assets, the government used the legal system, tax authorities and environmental agencies to put pressure on private shareholders to surrender control. The government also promoted its own people to the positions of power in state owned enterprises allegedly based on the individuals' loyalty and not their ability to improve operational efficiency. Key details of reported control disputes are presented below:

- The government was seeking to re-establish control over AvtoVaz by opening and closing criminal investigations and bringing in a symbolic suit against the joint-venture partner General Motors (AvtoVaz).
- It was suggested that Ryazanov (Gazprom Deputy CEO) became so powerful that he started to represent a threat to some other high-ranking officials within Gazprom and the government. Ryazanov was replaced with an ex-KGB agent from St. Petersburg who worked at the mayor's office at the same time as Putin (Gazprom).
- The government arbitrarily imposed back tax-bills on Yukos in an effort to seize control over its main assets. The decision was linked to Khodorkovsky's support of political opposition. The case was disputed in local and international courts (Yukos).



- A subordinate refused to follow the orders of his superior who represented the interests of the sole shareholder of an international unit of Yukos. Instead of the proposed appointment, the person who was fired received promotion. Analysts suggested that such an act of insubordination would have been impossible without the support of the government and/or high-ranking officials from Rosneft (Yukos).
- The government was seeking to re-establish control over the country's oil and gas industry. The government used the Federal Service for Ecological, Technological and Atomic Inspection to force ExxonMobil to renegotiate terms of the Production Sharing Agreement (ExxonMobil).
- The government used environmental violations and non-compliance with the license agreement to force TNK-BP to accept 'Gazprom tailored' terms of restructuring (TNK-BP).

#### 2.1.6.1 Implications for the Rule of Law with Reference to Control Disputes

Analysis of this type of corporate dispute suggests that previously weak property rights have become noticeably stronger. In 2006 there were no reported instances of privately initiated seizures of control of corporate entities that are only possible in the environment where formal institutions completely lack enforcement powers and the central authority is weak. Situations similar to what happened to VimpelCom, Subway, Knauf AssiDoman, Trans World, and Kosmos TV in 1998 were not reported in 2006 and hence there are grounds to suggest that such disputes are regarded as the legacy of the past and are unlikely to be repeatable in the current context. Moreover, instances when control was transferred by means of an unfounded reduction of ownership stakes have also disappeared from the reports of the newspaper. Additionally, corporate culture has seemingly developed to such an extent that even powerful stakeholders have begun to respect the integrity of shareholder nominated agents. Previously there was a real danger that after a mutually agreed transfer of ownership rights such agents would not be accepted by their new stakeholders. Subsequently, control was challenged by virtue of that fact. By 2006 potential buyers had accumulated enough credibility (partially due to a more established status of prospective owners and less discounted sales) that instances of outright non-subordination subsided in prominence.

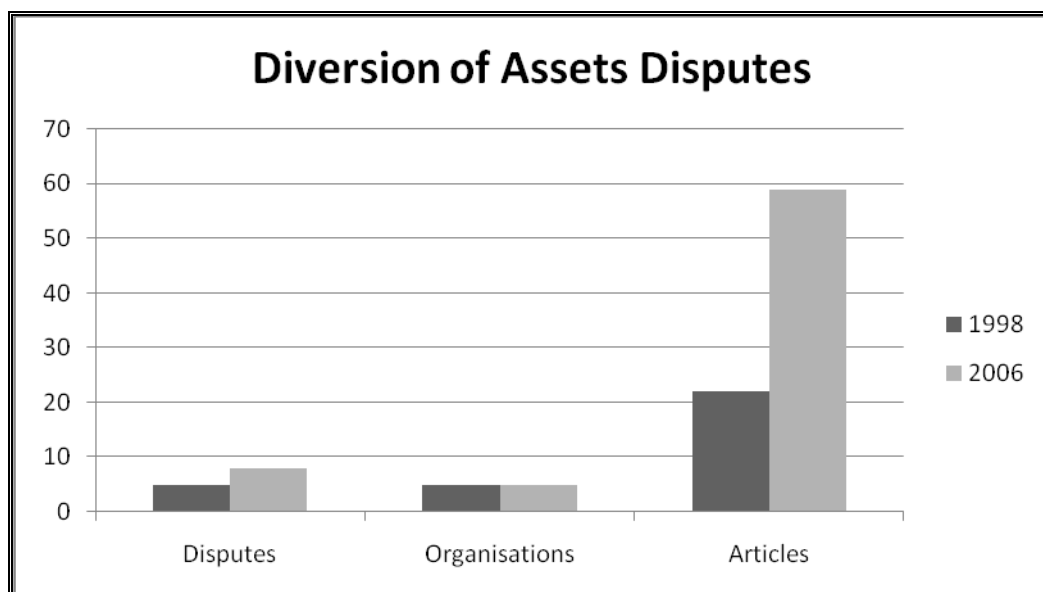
However, in 2006 the government reinforced its efforts to re-establish ownership and control over major assets. The government's tactics in achieving its goal particularly with regard to situations when there was an element of unwillingness to cooperate, was surprisingly reminiscent of the crudest forms of corporate misconduct reported in 1998. This grim conclusion suggests that those who violated norms of corporate behaviour in 1998 for the benefit of private parties, in 2006 were recruited by the Russian government to deal with the task of rearranging the balance of power and control in favour of the state.

## 2.2 Second Order Codes (Diversion)

### 2.2.1 Diversion of Assets

This category refers to situations when value of corporate assets is artificially depressed or de facto ownership of these assets is challenged. According to the reported data 5 disputes affecting 5 organisations occurred in 1998. Those were referred to in 22 articles published by the newspaper. In 2006, 8 disputes of this nature were identified. Further numerical information about this category is presented in graph 4.14.

Graph 4.14: *Diversion of Assets Disputes*



With reference to 1998 data, it can be observed that highly discounted sales took place at that time. As the example of Purneftegaz (Rosneft's subsidiary) demonstrates some assets were sold for less than one fortieth of the value established by alternative appraisers. Further details of disputes falling into this category are presented below:

- A 38 percent stake in Rosneft's subsidiary Purneftegaz was seized by creditors and sold for just \$10 million. However, according to analysts the value of the sold stake was between \$400 million and \$500 million (Rosneft).
- A large equity stake in a strategic natural-gas refining company was sold off to an unknown European company for roughly \$20 million, a price significantly below the company's value. Allegedly, the buyer was connected to Gazprom (Gazprom).
- Sibneft depressed the market price of its subsidiaries by means of transfer pricing and assets stripping before consolidation (Sibneft).
- A Russian joint-venture partner denied Subway access to some of its acquired assets (Subway).
- The state owned company used its powers to negotiate the lease agreement in its favour depriving the foreign investor of any guarantees thus driving the foreign investor out of the project (MCCI).

In 2006 disputes arising as a result of inadequate valuations of assets continued to be perceived as a prominent feature of corporate environment in the country. The difference here is that in the late 1990s assets were transferred always from state-owned corporations, whereas in 2006 the trend reversed primarily in the direction of Gazprom and Rosneft who continued to buy assets at below market value. Although these companies are under greater scrutiny by international observers, that does not preclude them from diverting assets away from their potential rivals.

- Alleged asset stripping and transfer pricing took place at Rosneft's subsidiaries. The subsidiaries complained to the government. Rosneft acknowledged transfer pricing and asset stripping saying that the former was common practice within the oil industry and the latter was the result of Rosneft's major investment in the subsidiary (Rosneft).

- The Russian government and Rosneft's officials used IPO in London as an instrument for legitimising the status of controversially acquired assets previously belonging to Yukos (Rosneft).
- There was a diversion of assets and claims from Gazprom to Itera (the biggest independent gas producer in Russia) through crony deals valued at as much as \$4 billion a year and then back to Gazprom through a politically backed consolidation (Gazprom).
- The government decided to consolidate control over the oil and gas sector in the hands of Gazprom, yet delayed the law on strategic assets (Gazprom).
- The decision to get rid of two foreign Yukos managers was made by the court appointed Yukos receiver and enforced by means of an extraordinary shareholder meeting that was ruled to be legitimate by a Dutch court. The two managers were accused of trying to hide the company's assets (essentially from Rosneft) (Yukos).
- Valuations of Yukos assets were carried out in such a way as to suit Rosneft. A number of alternative (more independent), valuations including that by UBS, produced substantially higher figures (Yukos).
- Shell and its Japanese partners were forced to accept Gazprom's entry into its Sakhalin 2 project as a majority shareholder because otherwise the government would have withdrawn several of its operating licences (Royal Dutch Shell).
- The Russian government used the Prosecutor General's Office and the Ministry for Natural Resources to come up with allegations against TNK-BP in order to pressurise the company into acceptance of a restructuring plan which involved Gazprom's participation (TNK-BP).

#### 2.2.1.1 Implications for the Rule of Law with Reference to Diversion of Assets Disputes

In connection with disputes arising as a result of diversion of assets, collected data demonstrates deterioration in both substance and amount of reported material. The culture of interfering with market regulated pricing of assets continues to be a prominent feature of the environment. In 2006 state-owned companies benefited a great deal from highly discounted purchases that private shareholders were forced to accept. Even though a blatant undervaluation has become more difficult

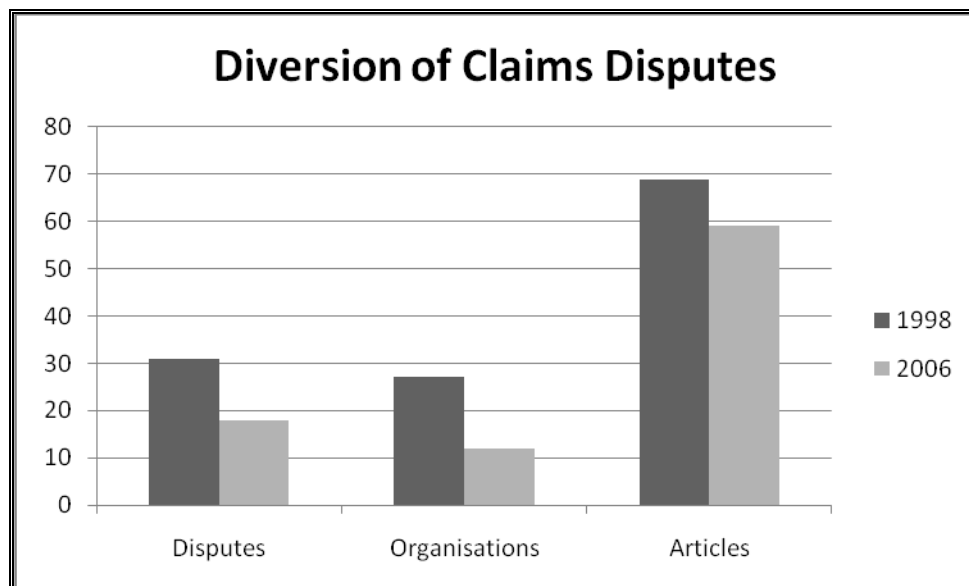
because of the participation of international stock exchanges in the process of financing large Russian enterprises, in terms of perception, this has had a minimal impact on how Russian companies go about acquisition of assets in the country.

### 2.2.2 Diversion of Claims

This category refers to situations when shareholders (and other stakeholders) are prevented from receiving a fair/proportionate financial remuneration for their exposure to a business entity. These situations occur when there are abnormal interferences that either diminish financial claims of shareholders directly through practices such as share dilution, or indirectly, by reducing a company's efficiency/profitability.

With regard to diversion of claims disputes there has been a reduction in the number of reported cases. This trend is in line with the overall reduction of the number of reported corporate disputes in 2006. Further numerical details of this category are presented in graph 4.15.

Graph 4.15: *Diversion of Claims Disputes*



Based on the 1998 data, diversion of claims was carried out primarily through share dilution. Companies in difficult financial circumstances need to raise additional capital and in the 1998 context this happened at the expense of less protected minority shareholders. There were instances when the minority appeared to have agreed to accept smaller stakes in healthier companies (e.g. KamAZ and Mosenergo), but in the majority of disputes new share emissions were used as a way of consolidating control on the cheap without any regard for the rights of practically unprotected minority shareholders (e.g. MGTS, Yukos, Sibneft, Sidanko, Lebedinsky Ore Mining Plant, etc). Secondly, insider dealings when resources were diverted by means of intermediary or management controlled companies (that benefited from questionable internal pricing arrangements) constituted a noticeable trend within the reported environment (e.g. Aeroflot, Gazprom, Yukos, Surgutneft, Channel 5, etc.). Further details of the diversion of claims disputes reported in the Moscow Times are presented in table 4.1.

Table 4.1: *Diversion of Claims Disputes, 1998*

<b>Company</b>	<b>Method of Diversion</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<b>Extent of coverage</b>			
<b>Aeroflot</b> (1 article)	Insider dealing	Majority shareholder of Aeroflot Boris Berezovsky	Travel agents and customers
<b>MGTS</b> (4 articles)	Share dilution	The Moscow city government	Minority shareholders
<b>AvtoVaz</b> (1 article)	Unjustified selling price	Dealerships	Shareholders of AvtoVaz and customers
<b>KamAZ</b> (2 articles)	Share dilution through issue of convertible bonds	Majority shareholders and the company in general	Minority shareholders and creditors
<b>KIA</b> (1 article)	Questionable tax allegations	Competitors	KIA shareholders

<b>Company</b>	<b>Method of Diversion</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<b>Extent of coverage</b>			
<b>Rosneft</b> (2 articles)	Transfer pricing and questionable write-offs of bad debts	Subsidiaries' top management	Shareholders of subsidiaries
<b>Gazprom</b> (1 article)	Barter schemes	Gazprom managers, connected stakeholders	Gazprom's minority shareholders
<b>Yukos</b> (10 articles)	Transfer pricing	Majority shareholders of Yukos (parent)	Minority shareholders of Yukos' subsidiary (inc. federal gov.)
<b>Yukos</b> (1 article)	Share issue	Directors (majority shareholders)	Minority shareholders
<b>Yukos</b> (1 article)	Interested party transaction (loan approval)	Shareholders of Yukos	Minority shareholders of Yukos' subsidiary
<b>Yukos</b> (1 article)	Questionable debt swap	Shareholders of Yukos	Shareholders of Yukos's subsidiary
<b>Yukos</b> (1 article)	Share dilution	Shareholders of Yukos	Creditor who received a stake as collateral
<b>Transneft</b> (7 articles)	Managers forced employees to sell their stakes at a discount	Top management of Transneft	Minority shareholders of Transneft (employees)
<b>Surgutneft.</b> (2 articles)	Share dilution and transfer pricing	A group of local 'investors' and St. Petersburg administration	Shareholders of parent (Surgutneft.)
Sibneft (5 articles)	Closed share issue	Majority shareholders of Sibneft	Minority shareholders of Sibneft's subsidiary
<b>Sidanko</b> (6 articles)	Share dilution through a closed bond issue	Majority shareholders	Minority shareholders

<b>Company</b>	<b>Method of Diversion</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<b>Extent of coverage</b>			
<b>Krasnoyarsk Hydro Plant</b> (4 articles)	Share dilution	Minority shareholder (Tanako FIG)	Shareholders of parent company (UES)
<b>UES<sup>61</sup></b> (1 article)	Non payment of promised dividends	Management of UES	Shareholders of UES
<b>Mosenergo</b> (1 article)	Share dilution	Mosenergo	Minority shareholders (foreign investors)
<b>Norilsk Nickel</b> (1 article)	Share dilution through closed share issue	Ordinary shareholders	Preferred shareholders (institutional investors)
<b>Novolipetsk</b> (3 articles)	Transfer pricing	Minority shareholder (Trans World)	Remaining Novolipetsk shareholders
<b>Lebedinsky Ore Mining Plant</b> (1 article)	Share dilution through charter capital increase	Management of the plant and regional administration of Begorod	Minority shareholder (Rossiisky Kredit Bank)
<b>SBS Agro</b> (4 articles)	Default on credit repayment	SBS Agro	Foreign creditors (Lehman Brothers)
<b>MOST Bank</b> (1 article)	Unauthorised transactions	Uneximbank	MOST Bank
<b>Pioneer Group</b> (1 article)	Unauthorised transactions	Small Russian bank 60% owned by Pioneer Group	Pioneer Group
<b>Tokobank</b> (1 article)	Refusal to honour futures contracts	Tokobank	A large group of Russian and foreign investors

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<sup>61</sup> United Energy Systems



<b>Company</b>	<b>Method of Diversion</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<b>Extent of coverage</b>			
<b>Rossiisky Kredit</b> (1 article)	Refusal to transfer money to customer's account	Rossiisky Kredit	Computer firm Trekhmernaya Pamyat
<b>Channel 5</b> (1 article)	Transfer pricing through unprofitable advertising contracts	Premier SV and LISS – advertising agencies owned by a well connected businessman (Lisovsky)	Channel 5 shareholders
<b>ORT</b> (1 article)	Share transfer as a political gesture allegedly to bribe Yeltsin	Yeltsin and Berezovsky	Shareholders of ORT
<b>Standart NMT</b> (1 article)	Unjustified increase of price of security services	A St. Petersburg police department	SME Standart NMT
<b>Post Office</b> (1 article)	Pocketed revenues leading to a growing debt	Management of Post Office	The Railways Ministry

In contrast to 1998, in 2006 there was only one case of share dilution reported in the newspaper. This corporate dispute involved the IT and Communications minister Leonid Reiman who was accused of diluting the government and minority's stakes in a telecommunications company, Megafon. The minister denied the allegation, but an arbitration tribunal in Zurich attributed this misappropriation to the government official. Other prominent examples of disputes falling into the diversion of claims category refer to the highly non-transparent re-nationalisation of key Yukos assets and re-negotiation of Production Sharing Agreements where the state-controlled companies like Rosneft and Gazprom emerged as clear winners at the expense of foreign and private entities like Total and LUKoil.

Table 4.2: *Diversion of Claims Disputes, 2006*

<b>Company</b>	<b>Method of Diversion</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<b>Extent of coverage</b>			
<b>Aeroflot</b> (1 article)	Purchasing strategy aimed at creating political allies and not shareholder wealth maximisation	Federal government	Minority shareholders of Aeroflot
<b>MegaFon</b> (2 articles)	Share dilution	IT and Communications Minister Leonid Reiman	The state and remaining shareholders of Megafon
<b>Rosneft</b> (2 articles)	Share transfer through a non-transparent middle company	Rosneft shareholders, the Russian state, political elite	Shareholders of Yukos
<b>Rosneft</b> (3 articles)	Under-valuation of subsidiaries in the wake of consolidation	Rosneft shareholders i.e. the Russian government	Shareholders of Rosneft's subsidiaries
<b>Rosneft</b> (2 articles)	Transfer pricing and assets stripping	Rosneft and the Russian government	Shareholders of Rosneft's subsidiaries
<b>Rosneft</b> (6 articles)	Acquisition of discounted Yukos assets	Rosneft and the Russian government	Shareholders of Yukos
<b>Gazprom</b> (1 article)	Transfer of assets from Gazprom to Itera and vice versa.	Management of Gazprom and Itera	Shareholders of Gazprom
<b>Gazprom</b> (4 articles)	Refusal to honour supply contracts	Gazprom and the Russian government	Customers (Ukraine, Belarus)
<b>Yukos</b> (23 articles)	Share transfers	Old Yukos shareholders	New shareholders of Yukos, i.e. Rosneft
<b>Yukos</b> (1 article)	Insider dealing	Gazprombank	Old shareholders of Yukos
<b>Total</b> (2 articles)	Re-negotiation of PSA agreements	Government-controlled oil	Shareholders of Total

<b>Company</b>	<b>Method of Diversion</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<b>Extent of coverage</b>			
		companies	
<b>LUKoil</b> (2 articles)	Valuation of subsidiaries	Shareholders of LUKoil	Shareholders of LUKoil subsidiaries
<b>Novolipetsk</b> (1 article)	Internal pricing	Majority shareholder of Novolipetsk	Minority shareholders of Novolipetsk
<b>Severstal</b> (2 articles)	Internal pricing	Majority shareholder of Severstal	Minority shareholders of Severstal
<b>RusAl</b> (1 article)	Valuation of subsidiaries	Majority shareholders of RusAl	Minority shareholders of RusAl
<b>RusAl</b> (1 article)	Corrupt bidding for assets	RusAl and Nigerian president	BFI Group Devino and Alcon shareholders
<b>Eurocement</b> (1 article)	Internal pricing	Majority shareholders of Eurocement	Minority shareholders of Eurocement (Russia Partners)
<b>IKEA</b> (4 articles)	Closure of a mall by health and safety inspectors	IKEA's competitors	IKEA

### 2.2.2.1 Implications for the Rule of Law with Reference to Diversion of Claims Disputes

Similar to previous categories, collected data suggests both positive and negative changes within the perceived environment as constructed by reported material.

In 2006, it was the government that instigated the practice of diverting claims by means of state controlled entities (except for the two privately initiated conflicts involving Eurocement and IKEA). In terms of the methods employed by the government nominated managers, this practice took the form of the most daring expropriation. With reference to Yukos, the most valuable assets of the company were transferred to Rosneft through an intermediary entity that was registered in the same building as a grocery shop. The intermediary company called the Baikal Finance Group received the assets previously belonging to Yukos, and later transferred those to the balance sheet of Rosneft. The scheme was devised to re-divert legal risks away from Rosneft and was criticised for a complete lack of transparency and accountability. Analysts alleged that a substantial amount of money changed hands during this transaction. The scheme involving transfer of assets from Gazprom to Itera and vice versa was very similar in style and extent of expropriation which was measured in billions of dollars. In 1998 similar expropriating practices took place. Barter schemes, illegal debt swaps, unprofitable contracting, ubiquitous share dilution and transfer pricing were constantly featured in the Moscow Times reports with reference to the most reputable companies. In both years of the investigation, minority shareholders appear to be the biggest losers in these conflicts, unable to defend their interests through the courts and other formal institutions. However, with regard to the main beneficiaries of these actions, there has been a shift away from private individuals who dictated the terms in 1998 in favour of the establishment that proved to be very much in control in the more recent year of the study.

However, with reference to conflicts involving solely private shareholders, there has been a noticeable positive change in the culture and extent of misappropriation. In 1998 collusion among a group of local investors (usually unidentified) and local administration was a force capable of attacking subsidiaries of even large corporate entities. Disputes involving Surgutneftegaz and

Lebedinsky Ore Mining Plant serve as an example of the type of corporate conflicts that in 2006 ceased to be directly associated with the perceived environment. Moreover, with reference to a number of 2006 disputes featuring transfer pricing as a method of diverting claims, constructive solutions have been proposed by key shareholders (Novolipetsk and Severstal) after the concerns raised by minority stakeholders. Encouraging examples of such preventive measures have not been found among the material reported in 1998. Finally, in 1998 and 2006, there were a number of disputes around valuation practices. In these instances dialogues between parent companies and shareholders of subsidiaries was on a more equal footing in the more recent year of the investigation. Blatant undervaluation exemplified by the management-controlled consolidation of Transneft in 1998 has been replaced by a more balanced negotiating process that took place during LUKoil's consolidation in 2006.

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## Section 3: Analysis of the Content of the Third Order Codes

In this section, the content of the third order codes is analysed. A graphical representation of each code and relevant themes are provided. The data is presented in tables followed by a comparison of key elements of the two years.

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### 3.1 Third Order Codes (Disputes)

Third order codes<sup>62</sup> further define corporate disputes making it possible to capitalise on the richness of the gathered data. In addition to the overall patterns revealed by the analysis of the second order codes, this section offers intricate details and complementary characteristics of the identified corporate disputes. Moreover, the hierarchical nature of the data is revealed in this section by providing a link between second and third order codes with reference to the categories (bar charts) and separate disputes (tables).

#### 3.1.1 State Interference

State interference occurs when federal and local governments become a party to corporate disputes. Clearly the state can have a variety of motives for being actively involved in corporate affairs other than financial gain. Comparison of this category therefore should reveal the perceived change in such motives as well as outline the evolving nature of state participation in corporate life in Russia.

In total 25 disputes<sup>63</sup> were coded as state interference in 1998. All second order codes are represented within this category apart from bankruptcy disputes. Disputes coded as ownership, taxes and control produced the most active participation of the state (see graph 4.16) whereas disputes coded as diversion of claims featured only one instance of state interference. Further details of this category are summarised in table 4.3 specifying reasons for state interference, prevailing stakeholders and relevant comments.

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<sup>62</sup> In total there are five third order codes: State Interference, Inadequate Information, General Meetings, Unclear Rules and Transactions with Self-Interest.

<sup>63</sup> Altogether, there were 19 individual disputes of which 6 were parallel coded.

Graph 4.16: *State Interference 1998*

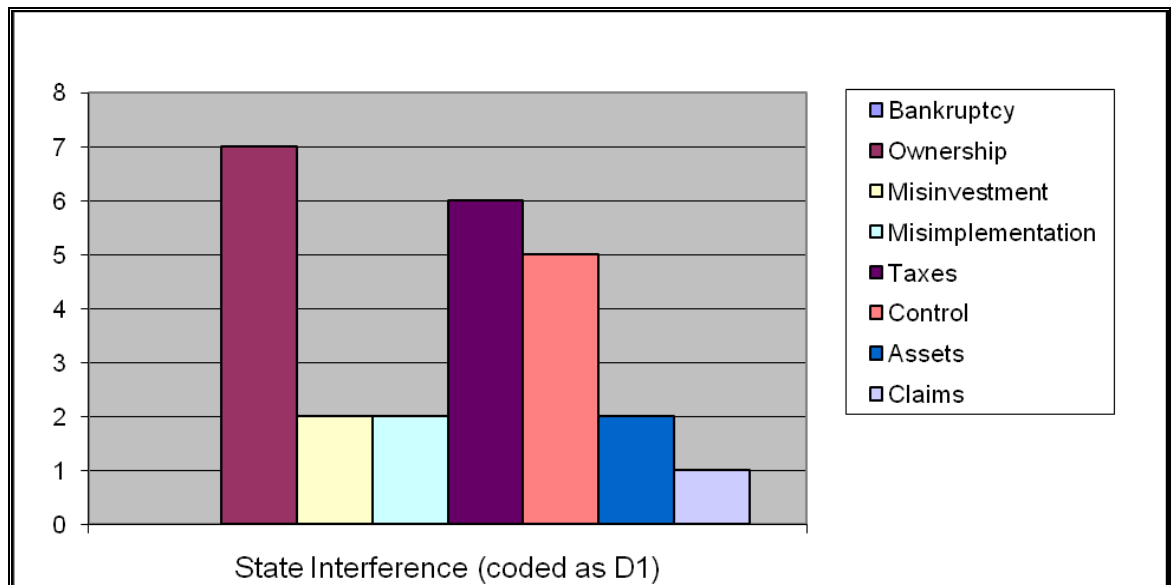


Table 4.3: *State Interference, 1998*

Company	Reasons for State Interference	Prevailing Party	Comments
<i>Template Details Appendix 9a</i>			
<b>Gaz</b> <i>1 Article, ref. 7</i> <i>Coding<sup>64</sup>: Taxes</i>	Encourage investment by offering tax breaks	IMF	Tax breaks were withdrawn because they fell foul of IMF requirements
<b>Rosneft</b> <i>8 Articles, ref. 10.1</i> <i>Coding: Diversion of Assets</i>	Return of a valuable stake in a Rosneft's subsidiary that had been sold on by creditors	The government	Technically the creditors had a right to sell the asset because Rosneft fell behind on debt repayments
<b>Gazprom</b> <i>1 Article, ref. 11.1</i> <i>Coding: Ownership</i>	Ownership restriction	Management-controlled intermediary companies and foreign investors	The government failed to enforce a ban on ownership of Gazprom shares by foreign investors

<sup>64</sup> The referenced 2<sup>nd</sup> order codes reveal the coding history of each dispute.

<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>			
<b>Gazprom</b> <i>3 Articles, ref. 11.2 Coding: Taxes</i>	Tax claims against the company	Tax authorities who froze accounts of two Gazprom subsidiaries	The Duma protested by declaring the action a threat to national security
<b>Gazprom</b> <i>1 Article, ref. 11.3 Coding: Ownership</i>	Making the gas industry more accessible to foreign investors	The World Bank	The Russian government was under pressure from the World Bank to strip Gazprom of its monopoly status. The World Bank used the possibility of a loan as a bargaining tool
<b>Gazprom</b> <i>1 Article, ref. 11.4 Coding: Ownership</i>	Elections	Oligarchs and the government	Gazprom grew its media portfolio in order to ensure pro-Kremlin coverage
<b>Gazprom</b> <i>1 Article, ref. 11.5 Coding: Misinvestment</i>	Balance of power	The government	Head of Gazprom (Vyakhirev) fell out of favour with the government which used the Audit Chamber to cancel the original trust agreement.
<b>Yukos</b> <i>10 Articles, ref. 12.1 Parallel Coding: Control/Diversion of Claims</i>	Transfer pricing organised by Yukos management that negatively affected the government's stake	The government	The FSC cancelled the decision of a shareholders meeting that gave Yukos executives too much power.



<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>			
<b>Yukos</b> <i>2 Articles, ref. 12.6 Coding: Misimplementation</i>	Political context of the joint venture between Yukos and Sibneft	N/A	CEO of Yukos (Khodorkovsky) kept a low political profile. He pulled out of the planned merger after Berezovsky (alleged owner of Sibneft) made a number of controversial political statements.
<b>Sibneft</b> <i>1 Article, ref. 21.1 Parallel Coding: Control/Taxes</i>	Additional taxes	Local administration	Administration of the city of Omsk imposed an additional tax on the crude oil processed by a Sibneft refinery in order to increase its dwindling tax revenues.
<b>Sidanko</b> <i>4 Articles, ref. 22.2 Coding: Taxes</i>	Tax arrears	Tax authorities	The company was forced to settle its tax arrears because the government denied access to the export pipeline.
<b>Sidanko</b> <i>2 Articles, ref. 22.3 Parallel Coding: Taxes/Control</i>	Tax arrears	Sidanko	Local administration seized control of a Sidanko refinery for non- payment of taxes. The company responded by stopping supply of crude oil.
<b>UES</b> <i>11 Articles, ref. 25.1 Coding: Control</i>	Battle for leadership of the company	First deputy Prime Minister Nemtsov	Infighting between reform- oriented and more conservative political clans affected the company's leadership.

<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>			
<b>UES</b> <i>8 Articles, ref. 25.4 Coding: Ownership</i>	Ownership restriction	The Russian parliament <sup>65</sup>	The Russian parliament passed a controversial piece of legislation that limited ownership of foreign investors in UES to 25% despite a de facto ownership of 29%. The bill was a gesture of the communist dominated parliament aimed at spoiling Yeltsin's privatisation plans.
<b>Norilsk Nickel</b> <i>1 Article, ref. 28.3 Coding: Taxes</i>	Tax arrears	Norilsk Nickel	The company successfully contested a back-tax claim that represented the government's efforts to reduce the budget deficit.
<b>Lebedinsky Ore Mining Plant</b> <i>2 Articles, ref. 34.1 Coding: Ownership</i>	Contested ownership	Majority shareholder Nacosta	The government's stake in the plant was questioned in the courts. This fact upset the plans to raise the much-needed capital from the sale.
<b>SBS Agro</b> <i>1 Article, ref. 40.3 Coding: Misinvestment</i>	Support for banks affected by the financial crisis	SBS Agro	The decision to support some banks and not others was based on political affiliations and not performance related measures.

<sup>65</sup> At the time the Russian parliament was dominated by the opposition and therefore very often acted contrary to what the government proposed.

<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>			
<b>Kuznetsky Mine</b>  <i>1 Article, ref. 54 Parallel Coding: Ownership/ Misimplementation</i>	Contested ownership	Kemerovo authorities	Local authorities sought to get control over the newly renovated mine.
<b>MCCI</b>  <i>1 Article, ref. 55 Parallel Coding: Control/Ownership/ Diversion of Assets</i>	Lease agreement	State company GlvUpDK	A state company GlavUpDK had reneged on its part of the contract with MCCI by not turning over a lease on the property to the joint venture.

From the analysis of the summary table above, three main themes become apparent. First, in 1998 the government (being a hostage to the significant budget deficit) strongly depended on financial support from organisations like the IMF and the World Bank. However, this support came with certain conditions that the government had to meet. Improved tax collection was one of such conditions. It is for this reason that the government retracted its promise of tax breaks to the GAZ-Fiat venture and imposed additional tax liability on companies like Gazprom, Sibneft and Sidanko. Another condition imposed by the Word Bank was the opening up of key strategic sectors such as gas and electricity. In other words, if the government did not reform those sectors to the liking of international finance providers, financial support would not have materialised. From the view point of foreign investors it was a reassuring fact because in an instance of a large corporate scandal considerable pressure could have been applied to the government.

Second, in 1998 there were instances when the government acted as a minority shareholder fighting practices such as asset stripping and share dilution. These practices were initiated by parent companies which were controlled by a handful of oligarchs. A new share issue at Yukos, the sale of a stake in Purneftegaz (Rosneft's subsidiary) and Krasnoyarsk Hydro are examples of such daring

actions initiated by the financial industrial groups. Even though the government sometimes challenged these actions, a lot of newspaper 'noise' was generated by these disputes, frequently exposing the government's inability to protect its own interests (Lebedinsky Ore Mining Plant).

Lastly, disputes reported in 1998 demonstrate that the government was incapable of acting in unison because of the heated internal battles for control of large state companies such as UES (on the federal level) and Krasnoyarsk Hydro Plant (on the local level).

In 2006 26 reported disputes<sup>66</sup> featured state interference. Similar to 1998, all categories (apart from misinvestment) could be found within the hierarchy. Ownership, however, appeared as the most prominent second order code with ten separate disputes involving state participation<sup>67</sup>. In terms of the overall perception, this is a considerable number particularly in the context of the overall reduction of reported material covering corporate disputes. Furthermore, disputes involving Yukos (ownership, control and taxes) and Shell (ownership, diversion of assets and misimplementation) need to be highlighted as the most significant in terms of shaping investor perception because of the considerable amount of coverage received (23 and 25 articles respectively). Further details of this category are presented in graph 4.17 and table 4.4.

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<sup>66</sup> In total there were 16 individual disputes of which 10 were parallel coded.

<sup>67</sup> This has already been discussed with reference to ownership disputes.

Graph 4.17: *State Interference, 2006*

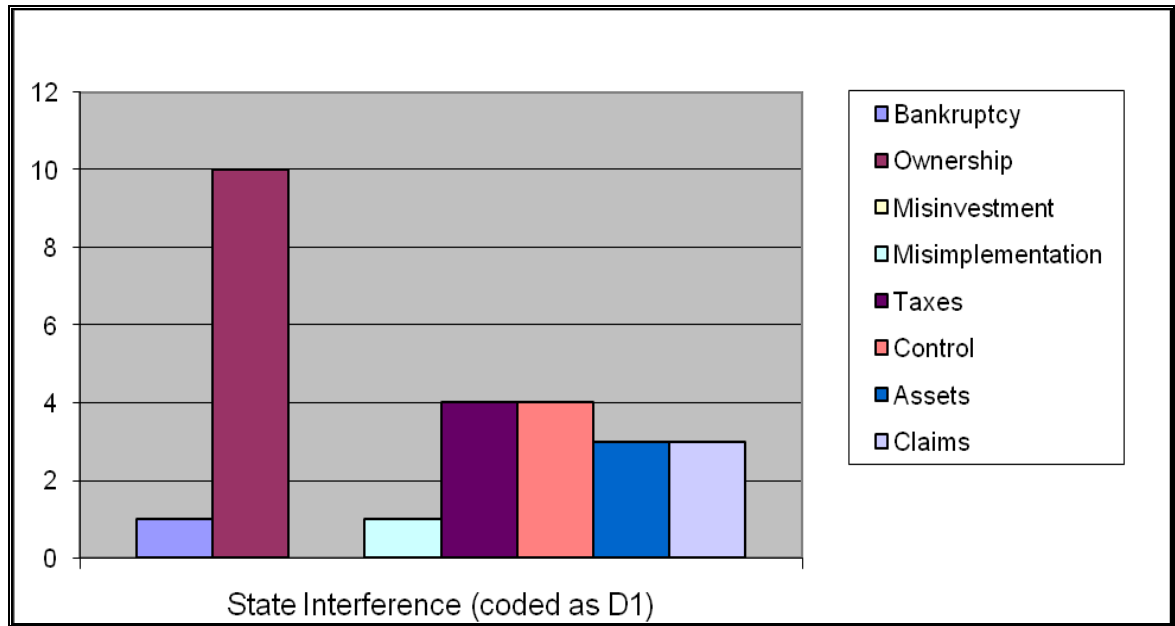


Table 4.4: *State Interference, 2006*

Company	Reasons for State Interference	Prevailing Party	Comments
<i>Template Details Appendix 9b</i>			
<b>Aeroflot</b> <i>1 Article, ref. 1 Coding: Diversion of Claims</i>	Recreation of the airline industry	The Russian government	The government looked for a politically acceptable partnership at the expense of the operational and financial efficiency.
<b>AvtoVaz</b> <i>2 Articles, ref. 6 Parallel Coding: Control/Taxes</i>	Appointment of state-friendly management	The Russian government	The government shifted the balance of power in the joint venture in its favour.
<b>Rosneft</b> <i>1 Article, ref. 10.4 Coding: Taxes</i>	Tax arrears and environmental violations	The Russian government	Nenets governor accused Rosneft of a \$33m. tax debt and breaking ecological standards. Subsequently, he was detained on suspicion of fraud and embezzlement.

<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>			
<b>Gazprom</b> <i>1 Article, ref. 11.1 Coding: Ownership</i>	Joint development of a gas field	BASF and the government	Gazprom, with the government's support, did not honour the agreement signed in the 1990s with Moncrief Oil International to jointly develop Yuzno Russkoe Gas Field. Instead, Gazprom opted for a more politically acceptable partner BASF with whom it swapped assets.
<b>Gazprom</b> <i>4 Articles, ref. 11.3 Parallel Coding: Diversion of Assets/ Ownership</i>	Building up the monopoly status	Gazprom (state controlled)	The government picked Gazprom as the national leader and started to put pressure on foreign oil majors to accept Gazprom's entry as a majority shareholder.
<b>Gazprom</b> <i>4 Articles, ref. 11.5 Parallel Coding: Diversion of Claims/ Ownership</i>	Export contracts	Gazprom and RosUkrEnergo (state controlled)	Gazprom renegotiated terms of supply contracts with Ukraine. The deal involved a non-transparent intermediary company.
<b>Yukos</b> <i>23 Articles, ref. 12.1 Parallel Coding: Ownership/ Control/ Taxes</i>	Fighting political opposition and restructuring oil and gas industry	Rosneft (state controlled)	The government was (internationally) accused of conspiring to expropriate Yukos with questionable back taxes allegations.

<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>			
<b>Yukos</b> <i>8 Articles, ref. 12.4 Coding: Bankruptcy</i>	Charges to prevent the sale of a refinery	The government and Rosneft	In order to make sure that Yukos did not find a way to avoid bankruptcy, the government initiated a set of new charges (may be legitimate) and used the Prosecutor General's Office and the Russian courts to prevent the sale of the Mazeikiu refinery.
<b>Shell</b> <i>25 Articles, ref. 13 Parallel Coding: Misimplementation/ Ownership/ Diversion of Assets</i>	Renegotiation of Production Sharing Agreements	Gazprom and the government	The government helped Gazprom enter the Sakhalin 2 project by accusing Shell of environmental violations. The environmental allegations were used as a bargaining tool to ensure favourable terms for Gazprom's entry.
<b>Total</b> <i>2 Articles, ref. 14 Parallel Coding: Ownership/ Diversion of Claims</i>	Renegotiation of Production Sharing Agreements	Gazprom and the government	The subsoil resource agency accused Total of inflating costs and producing too little oil and thus breaking the terms of the license agreement. The campaign against Total coincided with the government's push for greater state participation in major oil projects and contradicted previous agreements.
<b>ExxonMobil</b> <i>2 Articles, ref. 15 Coding: Control</i>	Renegotiation of Production Sharing Agreements	Gazprom and the government	The Federal Service for Ecological, Technological and Atomic Inspection accused ExxonMobil of a number of violations. The pressure coincided with the government's drive to renegotiate terms of major PSA agreements.

<b>Company</b>	<b>Reasons for State Interference</b>	<b>Prevailing Party</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>			
<b>TNK-BP</b> <i>15 Articles, ref. 16.1 Parallel Coding: Ownership/ Control/ Diversion of Assets</i>	Reallocation of major development licences	Gazprom and the government	The government used the Prosecutor General's Office and the Ministry for Natural Resources in order to pressurise TNK-BP into its acceptance of the restructuring plan which involved Gazprom's participation in the massive Kovykta gas project.
<b>TNK-BP</b> <i>1 Article, ref. 16.2 Coding: Taxes</i>	Reallocation of development licences	Gazprom and the government	The government threatened to withdraw TNK-BP's license to develop a gas field in West Siberia. The allegations coincided with Gazprom's speculated purchase of the stake belonging to a number of Russian oligarchs (TNK).
<b>LUKoil</b> <i>2 Articles, ref. 17.1 Coding: Ownership</i>	Establishing control over oil and gas industry	The government	The government relied on the Natural Resources Ministry's environmental regulator to prevent aggressive bidding and force LUKoil into sharing licenses.
<b>Transneft</b> <i>2 Articles, ref. 18 Coding: Ownership</i>	Abuses of power by former managers	The government	The government, being a majority shareholder in Transneft, began an investigation into abuses of power by previous managers during privatisation of the company. The investigation was allegedly stemming from a conflict of a political nature.
<b>Evrax</b> <i>1 Article, ref. 31.2 Coding: Ownership</i>	Evrax's bid for Oregon Steel	N/A	The US authorities scrutinized links between Abramovich and the Russian Government in relation to Evrax's bid for Oregon Steel. It was suspected that the former was acting on the orders of the latter.



According to the reported material in 2006, all corporate disputes involving state participation serve as a vivid demonstration of the unchallenged power of the authorities. In the most recent year of the investigation the government emerged as a clear winner in all reported corporate disputes. The way in which the government dismantled Yukos<sup>68</sup>, restructured the largest oil projects (Shell, TNK-BP, LUKoil), and selected politically acceptable partners (Aeroflot and Gazprom) demonstrates the newly established authority of the state which is not only capable of challenging large financial corporations, but also reaching out to the regions punishing local opposition (see Rosneft, reference 10.4 for additional details).

#### 3.1.1.1 Implications for the Rule of Law with Reference to State Interference Disputes

Comparison of the state interference disputes does not unequivocally suggest that the perception of the rule of law improved along this dimension. Conversely, based on the coded data presented above, the newly re-established authority of the state in 2006 was likely to have been perceived as a threat by foreign investors and not a sign of an improved environment. Despite the severely unpredictable context, in 1998 corporate assets were being continuously released from the government's grip creating unprecedented opportunities for private and foreign investors. In 2006 this trend reversed in favour of the government thus depriving private shareholders of access to a large amount of key assets. However, in both years of the study the government's motives appear to be rather self-centred. The only stark difference is in the effectiveness with which the Russian government pursued its interests.

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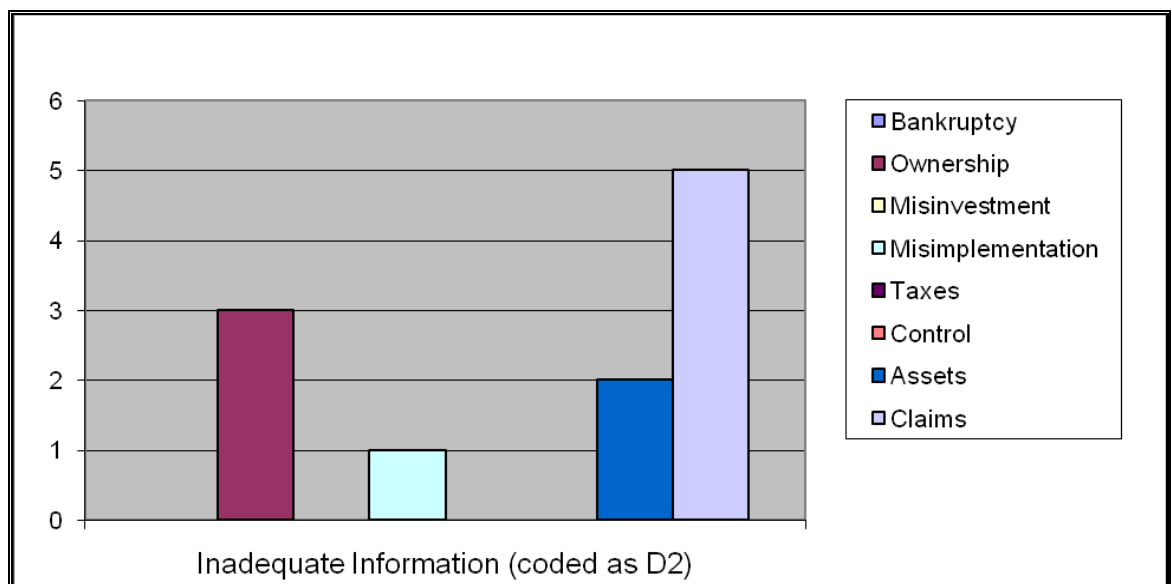
<sup>68</sup> An interesting point is that Khodorkovsky (CEO and majority shareholder of Yukos) in 1998 had the image of a politically detached businessman famous for his aggressive treatment of minority shareholders. In 2006 that image was drastically changed (particularly in the western media) to a Russian version of Mandela i.e. a liberal fighter for political freedom and corporate justice.

### 3.1.2 Inadequate Information

Inadequate information is a category that refers to corporate disputes that feature an inappropriate level of communication between management and key stakeholders. In the corporate governance context examples of such poor communication could be a refusal to disclose ownership structures, incorrect/incomplete financial reporting and corporate releases, undisclosed sales and unadvertised share issues.

In 1998 there were 11 examples<sup>69</sup> of poor corporate communication with diversion of claims being the most frequent second order code. There were no reported instances of inadequate information in conjunction with bankruptcy, misimplementation, taxes and control disputes. Further details of the reported instances of this category are presented in graph 4.18 and table 4.5.

Graph 4.18: *Inadequate Information, 1998*



<sup>69</sup> In total there were 11 separate disputes (no parallel coding).

Table 4.5: *Inadequate Information, 1998*

Company	Inadequate Information	Benefiting Party	Disadvantaged Party
<i>Template Details Appendix 9a</i>			
<b>MGTS</b>  <i>4 Articles, ref. 3 Coding: Diversion of Claims</i>	Investor tender agreement (permitting a majority shareholder new share emission) did not appear in the investment prospectus	Majority shareholder (the Moscow Committee for Science and Technology)	Minority shareholders
<b>Rosneft</b>  <i>8 Articles, ref. 10.1 Coding: Diversion of Assets</i>	Identity of a purchaser of a 38% stake in Purneftegaz (Rosneft's subsidiary) was unknown <sup>70</sup> . The stake was sold for a fraction of its estimated value.	Unknown	Rosneft
<b>Gazprom</b>  <i>1 Article, ref. 11.6 Coding: Diversion of Assets</i>	A large equity stake in a strategic natural-gas refining company was sold off to an unknown European company for roughly \$20 million, a price significantly below the company's value. No information about the buyer was made available by privatization officials although Gazprom's involvement was suspected.	Gazprom	Minority shareholders

<sup>70</sup> The identity of the behind-the-scenes company was unknown, although sources in the media mentioned LUKoil, oligarch Boris Berezovsky and former Rosneft managers. An investigation by The Moscow Times traced possible links to LUKoil and Kremlin insider Pavel Borodin, while another possible buyer of the stake was directly related to the heads of the Russian Orthodox Church.

Company	Inadequate Information	Benefiting Party	Disadvantaged Party
<i>Template Details Appendix 9a</i>			
<b>Yukos</b> <i>2 Articles, ref. 12.6 Coding: Misimplementation</i>	Undisclosed cash transfers, unaudited books, and questionable claims of proven oil reserves.	Majority shareholders (Khodorkovsky and Berezovsky)	Foreign investors and minority shareholders
<b>Transneft</b> <i>7 Articles ref. 18 Coding: Diversion of Claims</i>	The sale of Transneft's shares was conducted through non-transparent off-shore companies and one British company with an untraceable ownership. Appraisal of shares was completely flawed.	Management	Minority shareholders (workers)
<b>Surgutneftegaz</b> <i>2 Articles, ref. 19 Coding: Diversion of Claims</i>	Surgut's interest in three subsidiaries - Ruchi, Nefto-Kombi, and Krasny Neftyanik - was sold off for an undisclosed sum to a group of local 'investors.'	St. Petersburg administration and local 'investors.'	Parent company Surgutneftegaz
<b>Sibneft</b> <i>1 Article, ref. 21.3 Coding: Ownership</i>	The State Antitrust Committee failed to determine owners of Sibneft because investment banks could not be forced to disclose ownership information. Also, the company refused to disclose the identity of its majority shareholder (although according to numerous speculations in the media and among market analysts it was Boris Berezovsky).	Sibneft majority shareholders	Dart Management (minority shareholder of a Sibneft subsidiary whose ownership stake was under investigation <sup>71</sup> )

<sup>71</sup> The investigation was possibly linked to Dart's criticism of Russian corporate governance and more specifically his allegations against Sibneft's consolidation. There might have been an influential player - Berezovsky - behind the investigation.

Company	Inadequate Information	Benefiting Party	Disadvantaged Party
<i>Template Details Appendix 9a</i>			
<b>Sidanko</b> <i>6 Articles, ref. 22.1 Coding: Diversion of Claims</i>	The closed bond issue was not advertised to minority shareholders when they were buying in.	Majority shareholder	Minority shareholders
<b>Norilsk Nickel</b> <i>1 Article, ref. 28.2 Coding: Diversion of Claims</i>	Renaissance falsely reported that Norilsk shareholders had voted to approve a new closed share issue. Over the following two days, the share price of Norilsk preferred shares fell by more than 10 percent. Uneximbank ultimately relented and changed the terms of the issue which included preferred shareholders <sup>72</sup> .	Ordinary shareholders	Preferred shareholders
<b>SBS Agro</b> <i>3 Articles, ref. 33 Coding: Ownership</i>	Although the Central Bank had said SBS-Agro depositors could have access to their funds, it later retracted that pledge <sup>73</sup> .	SBS Agro	Depositors

<sup>72</sup> Investors suggested that the mistake was either a massive coincidence or a massive manipulation.

<sup>73</sup> It appears that unfulfilled promises by Sberbank to pay depositors were used to delay resolution and confuse the parties involved.

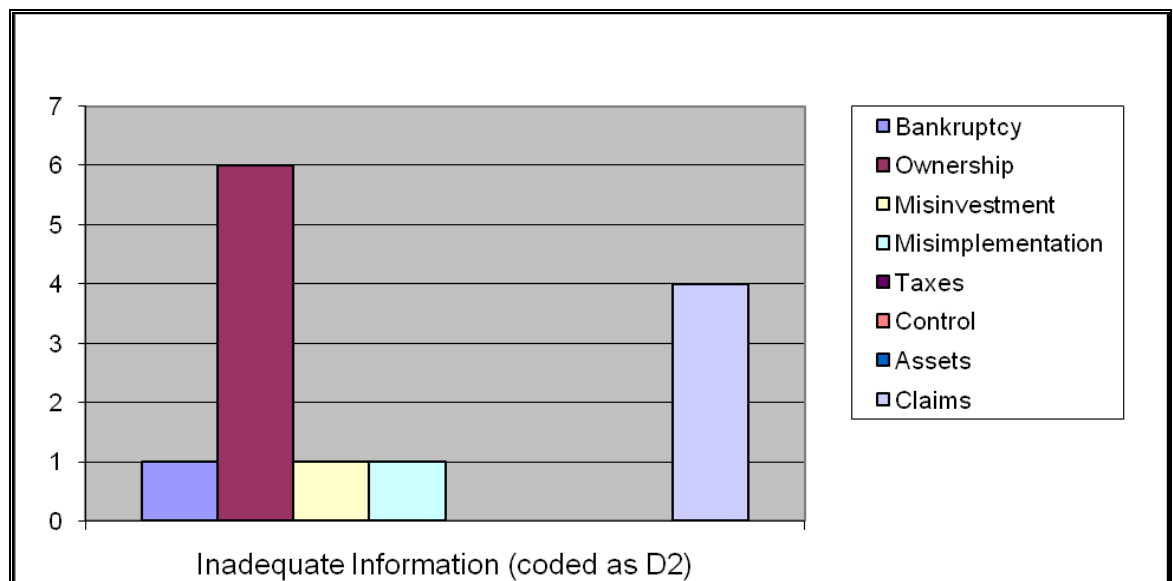
Company	Inadequate Information	Benefiting Party	Disadvantaged Party
<i>Template Details Appendix 9a</i>			
<b>Lomonosovsky Porcelain Factory</b>  <i>1 Article, ref. 53 Coding: Ownership</i>	Foreign investors claimed that they had determined that the St. Petersburg brokerages had the right to sell the shares, although they did not know the details of how the brokers acquired the shares of Lomonosovsky Porcelain Factory. A financial consultant to the factory, however, said the investors did not exercise due diligence when dealing with the brokerages, which were reported to have been involved in questionable stock transactions in the past <sup>74</sup> .	Potential Russian investors with strong contacts	Foreign investors

<sup>74</sup> Lomonosov was a closed joint-stock company, which meant a shareholder could not sell his shares to a third party without the consent from all shareholders. The shares were transferred through a scheme by which a factory employee gave one of his shares as a gift to an intermediary company, which thus became a shareholder and could buy any number of shares.

According to the above table, sacredly guarded identity of corporate owners was a prominent feature of the perceived environment in 1998. The most vivid example of such non-disclosure was the secret identity of a Sibneft's majority shareholder. Many speculated him to be Mr. Berezovsky, but the latter continuously denied his association with the company<sup>75</sup>. Moreover, disputes involving such companies as MGTS, Yukos, Sidanko and Norilsk Nickel demonstrate that systematic ambiguity around closed share issues made minority shareholders extremely vulnerable to a substantial dilution.

In 2006 the Moscow Times reported 13 disputes<sup>76</sup> involving inadequate information as defined above. Taxes, control and diversion of assets were not featured in the hierarchy of second order codes whereas the ownership category was the most widely represented. Further details of inadequate information disputes reported in 2006 are presented below in graph 4.19 and table 4.6.

Graph 4.19: *Inadequate Information, 2006*



<sup>75</sup> A fascinating fact is that despite such denials in the past, Mr. Berezovsky took the Russian government to court in 2008 over the price for which he was allegedly forced to sell his majority stake in Sibneft to Roman Abramovich.

<sup>76</sup> In total there were 11 individual disputes of which 2 were parallel coded.

Table 4.6: *Inadequate Information, 2006*

Company	Inadequate Information	Benefiting Party	Disadvantaged Party
<i>Template Details Appendix 9b</i>			
<b>Svyazinvest</b> <i>1 Article, ref. 2 Coding: Ownership</i>	The Russian government promised to privatize the remaining 75% stake in Svyazinvest, but kept delaying the sale <sup>77</sup> . Because of the uncertainty with privatisation a number of strategic investors (including George Soros) sold their stakes at a loss.	The government	Minority shareholders and potential investors
<b>VimpelCom</b> <i>1 Article, ref. 4 Coding: Misinvestment</i>	Telenor accused VimpelCom of providing misleading information to shareholders regarding VimpelCom's purchase of Ukrainian RadioSystems.	Alfa Group (owner of a blocking stake in VimpelCom)	Telenor (owner of a blocking stake in VimpelCom)
<b>MagaFon</b> <i>2 Articles, ref. 5 Parallel Coding: Diversion of Claims/ Ownership</i>	A Bermuda-based investment fund that controlled a significant proportion of Russia's telecoms industry continued to deny that IT and Communications Minister Leonid Reiman was one of its owners despite a Zurich court's claim to the contrary.	Alfa Group	Investment Fund IPOC and IT and Communications Minister Leonid Reiman

<sup>77</sup> The government broke its promise to sell a 75% stake in Svyazinvest to strategic investors because it was looking for a politically acceptable partner.



<b>Company</b>	<b>Inadequate Information</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<i>Template Details Appendix 9b</i>			
<b>Rosneft</b> <i>2 Articles, ref. 10.1 Coding: Diversion of Claims</i>	A 26.79 percent stake in Yugansk had been transferred to Rosneft's balance sheet from Baikal Finance Group <sup>78</sup> , an opaque shell company used to sidestep legal risks in a highly controversial government auction of Yukos' main production unit.	Rosneft and the government	Shareholders of Yugansk-neftegaz
<b>Gazprom</b> <i>4 Articles, ref. 11.5 Parallel Coding: Diversion of Claims/ Ownership</i>	All gas delivered to Ukraine, and some of the gas delivered to Europe, was handled by RosUkrEnergo, a Swiss-registered trading company with a dubious reputation that was half-owned by Gazprom. The other half was held by Raiffeisen Bank on behalf of a group of investors whose identities had not been disclosed.	Gazprom, Russian and Ukrainian officials.	Customers
<b>Yukos</b> <i>8 Articles, ref. 12.4 Coding: Bankruptcy</i>	There was a lack of information in the West about Yukos and GML assets, which, according to different estimates, total between \$5 billion and \$20 billion.	Rosneft and the government	Yukos' minority shareholders

<sup>78</sup>Baikal Finance Group was registered in the same building as a grocery store in the city of Tver.

<b>Company</b>	<b>Inadequate Information</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<i>Template Details Appendix 9b</i>			
<b>Transneft</b> <i>2 Articles, ref. 18 Coding: Ownership</i>	Detailed information about the owners of Transneft's preferred shares had to be disclosed because of an ongoing criminal investigation into abuses by former Transneft managers during the company's privatization <sup>79</sup> .	The government	Preferred shareholders
<b>Severstal</b> <i>4 Articles, ref. 30.2 Coding: Misimplementation</i>	Several European brokerages and investor consultancy groups criticized the speed with which Arcelor's management arranged the Severstal merger and the lack of information provided about the Russian company and its majority owner <sup>80</sup> .	Acelor	Severstal (Mordoshov)
<b>Evrz</b> <i>1 Article, ref. 31.2 Coding: Ownership</i>	The US authorities wanted to determine the nature of the relationship between the Russian government and Abramovich (majority shareholder of Evraz) before approving the Russian company's bid for Oregon Steel.	The US government	N/A

<sup>79</sup> Deutsche UFG suggested that asking brokerages to disclose beneficiary owners of the company's shares was 'an unprecedented case for the Russian stock market, which in our view will likely further worsen sentiment surrounding Transneft shares'.

<sup>80</sup> Arcelor's shareholders voted down Mordoshov's offer despite recommendations from the board. Mordoshov may have had an informal agreement with the board of Arcelor promising their support in return for some sort of compensation.

<b>Company</b>	<b>Inadequate Information</b>	<b>Benefiting Party</b>	<b>Disadvantaged Party</b>
<i>Template Details Appendix 9b</i>			
<b>RusAl</b> <i>3 Articles, ref. 32.3 Coding: Ownership</i>	The EBRD and IFC used the possibility of a corporate loan as a means of forcing RusAl to disclose its ownership structure <sup>81</sup> .	EBRD and IFC	Sole owner of RusAl Oleg Derepaska
<b>Eurocement</b> <i>1 Article, ref. 37 Coding: Diversion of Claims</i>	The American registered fund upset the majority owners of the Eurocement group by blocking new share issue. The majority owners responded by a refusal to send financial information to the fund.	Majority shareholder	Minority shareholder (American investment fund)

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<sup>81</sup> Further to the disclosure, a former business partner of Derepaska went for litigation to extract more money that he felt RusAl owed him. To address these concerns the company recruited two high-profile non-executive directors.

In 2006 there were examples when stakeholders received inaccurate/incomplete/misleading information. With the exception of VimpelCom and Eurocement however, it was the government who created such confusion by either abandoning promises to privatise a stake in Svyazinvest, or refusing to publicly disclose Yukos' financial flows. Similar to 1998, undisclosed ownership continued to be a characteristic of the Russian corporate environment. Owners of IPOC (Megafon), Baikal Finance Group, and RosUkrEnergo remained officially undisclosed in 2006 despite serious concerns from existing and potential investors.

### 3.1.2.1 Implications for the Rule of Law with Reference to Inadequate Information Disputes

Similar to the previous category no stark improvements occurred on this front. The environment in 2006 continued to be filled with secret entities with undisclosed ownership and unaudited financial information. In the instance of RosUkrEnergo, KPGM simply resigned as the company's auditor due to concerns over its own reputation<sup>82</sup>. The prominence of companies in question speaks volumes of the negative impact such non-disclosures had on investor perception of the rule of law in the country.

However, there was a positive example when a shareholder formally acknowledged the fact that he was a sole beneficiary in exchange for a corporate loan from the EBRD (RusAl). Although such a disclosure led to additional litigation instigated by previous business partners, hopeful investors could be forgiven for treating this as a sign of more possible disclosures of this nature in the future.

However, little change occurred in terms of the severity of misrepresentations with reference to purely corporate conflicts. In 1998 such a misrepresentation manifested itself through lack of information about new share issues. In 2006

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<sup>82</sup> An interesting fact is that according to reported material in 2007, PricewaterhouseCoopers in an unprecedented act withdrew their financial audits of Yukos further to a forceful request from the government. In general, this opens up a debate about integrity of even reputable auditors in the Russian context. The audit reports in question were over 8 years old and would not have been withdrawn had it not been for the government's interference. In general, private companies in Russia are keen to work with the big 5 in order to ensure access to international funding and improve their image abroad.

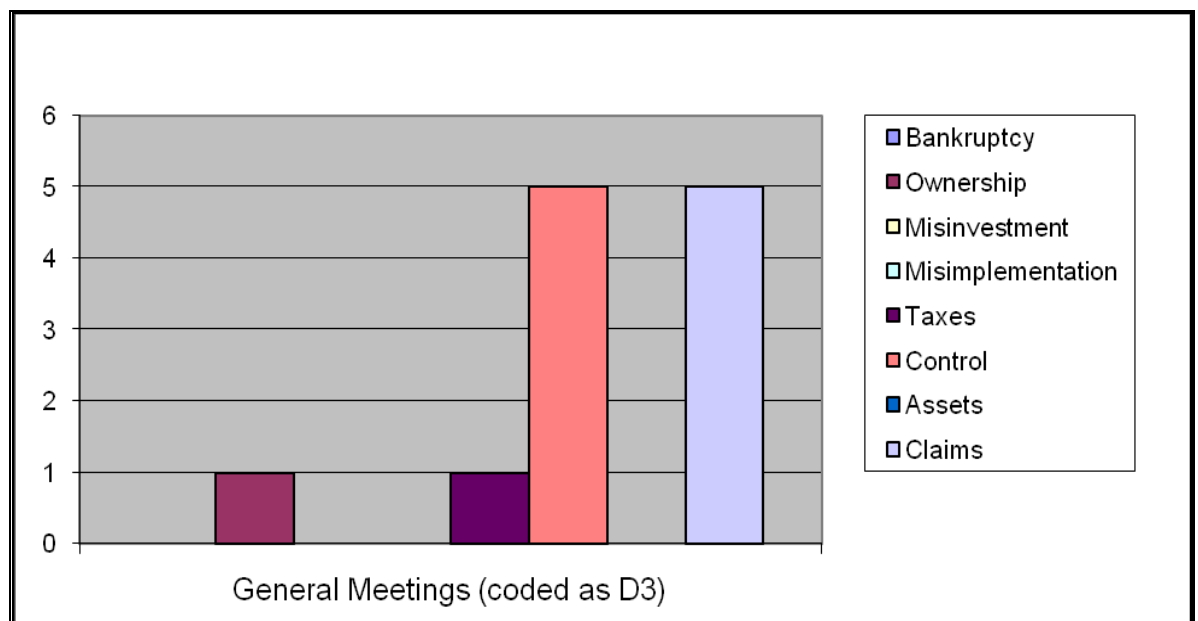
matching disputes involved intentionally misleading a corporate partner in relation to a proposed acquisition (VimpleCom) and a refusal to send financial information as a punishment for blocking a vote proposed by a majority shareholder (Eurocement).

### 3.1.3 General Meeting

This third order category refers to instances when important corporate decisions were made at general meetings of shareholders. The content of this category not only reveals the nature of corporate decisions at hand, but also shows how this crucially important corporate governance mechanism operates in the Russian environment.

In 1998 there were 12 disputes<sup>83</sup> reported in the Moscow Times in which general meetings played an important role in corporate proceedings. As opposed to previous third order categories, general meetings were most instrumental in disputes also coded as control and diversion of claims, see graph 4.20. Additional details of reported disputes featuring general meetings are presented in table 4.7.

Graph 4.20: *General Meetings, 1998*



<sup>83</sup> 10 individual disputes of which 2 were parallel coded.

Table 4.7: *General Meetings, 1998*

<b>Company</b>	<b>Issue (decision for approval)</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>		
<p><b>Rosneft</b></p> <p><i>1 Article, ref. 10.3</i> <i>Coding: Control</i></p>	<p>The board of directors of a Rosneft's subsidiary was given authority to sell up to 50% of the company's assets.</p>	<p>Under the Joint Stock Company law, charter amendments require a 75 percent vote. Rosneft was able to get a favourable verdict due to the fact that only 75 percent of the subsidiary's votes were present at the meeting, thereby giving its 51 percent stake a 68 percent weighting. Finding the other 7 percent was a matter of bargaining and subtle stealth.</p>
<p><b>Yukos</b></p> <p><i>1 Article, ref. 12.2</i> <i>Coding: Diversion of Claims</i></p>	<p>Allow the board of directors to issue new shares without shareholder approval.</p>	<p>Proposal was voted down by suspicious minority shareholders.</p>
<p><b>Yukos</b></p> <p><i>1 Article, ref. 12.3</i> <i>Coding: Diversion of Claims</i></p>	<p>Authorise a subsidiary to guarantee a \$500 million foreign loan to Yukos.</p>	<p>The motion was passed by only 58.2 percent of voting shareholders, the vast majority of which represented Yukos interests. Arrowhead Enterprises Ltd., which claimed 12.3 percent of the voting stock of Yukos' subsidiary Samaraneftegaz, alleged that the vote violated Russian joint-stock law. The Federal Securities Commission was asked to investigate the matter.</p>
<p><b>Yukos</b></p> <p><i>1 Article, ref. 12.8</i> <i>Coding: Taxes</i></p>	<p>Transfer executive powers from Eastern Oil Co. to Yukos in response to bankruptcy of the former.</p>	<p>The decision was declared illegal by the Tomsk Regional Property Fund and the transfer was blocked.</p>

Company	Issue (decision for approval)	Comments
<i>Template Details Appendix 9a</i>		
<b>Surgutneftegaz</b>  <i>2 Articles, ref. 19</i> <i>Coding: Diversion of Claims</i>	Strike the parent off the charter documents.	A representative from Surgut (parent) was allowed into the meeting, though he was forbidden to participate. The reason was a faxed power of attorney letter, an act deemed in violation of the AGM procedures established by the subsidiary's management. The representative watched helplessly as Surgutneftegaz's stake in the company was diminished from 42 percent to 11 percent.
<b>Krasnoyarsk Hydro Plant</b>  <i>4 Articles, ref. 24</i> <i>Parallel Coding: Diversion of Claims/Control</i>	Sale of a majority stake.	It was alleged that Krasnoyarskenergo's chief executive, Vladimir Kolmogorov, was not allowed to vote the company's 28 percent stake in the power plant because he had been elected at a general meeting that was declared invalid by a local court. KrAZ denied that there had been any irregularities at the meeting.
<b>Mosenergo</b>  <i>1 Article, ref. 26</i> <i>Coding: Diversion of Claims</i>	New share issue.	The decision made economic sense and was approved at a general meeting despite the fact that some minority holdings were diluted.
<b>Novolipetsk</b>  <i>4 Articles, ref. 29.1</i> <i>Coding: Control</i>	Nominations	Despite holding 40 percent, a group of investors was blocked from getting board representation at Novolipetsk. The old management clearly did not want to share power with the new shareholders, some of which appeared as a result of the controversial loan-for-shares deals. Once the court returned the ruling in favour of the shareholders, the old management attempted to avoid allowing the shareholders to vote in their representatives by removing voting from the agenda of the general meeting <sup>84</sup> .

<sup>84</sup> The culture of looking for loopholes and technical irregularities is very much visible in these sorts of conflicts. It appears that the spirit of the law is secondary to minor technicalities.

Company	Issue (decision for approval)	Comments
<i>Template Details Appendix 9a</i>		
<b>Knauf</b>  <i>1 Article, ref. 36.1</i> <i>Parallel Coding: Control/Ownership</i>	Challenging leadership and ownership of the company.	Sergiyenko was suspended from office by Knauf on allegations of theft, mismanagement and tax manipulation. His response was to hold his own meetings, physically remove Knauf from the building, and issue 64 percent new shares to dilute the Germans' stake. The local governor's office supported the share emission, saying it thought the factory should be re-nationalized.
<b>Inkombank</b>  <i>1 Article, ref. 42</i> <i>Coding: Control</i>	Dismantling the board of directors	Uneximbank-MFK prevented representatives from Inkombank from voting on dismantling the board due to an error on the part of the board. Inkombank representatives did not receive ballots for the vote. Inkombank successfully petitioned the St. Petersburg Arbitration Court for an injunction on the meeting. Even though initially the ruling was ignored, the decision of the court was eventually complied with upon delivery of the documents.

Analysis of the content of reported material belonging to this category unveils two main scenarios when general meetings were an integral part of corporate conflicts. The first scenario relates to decisions about the amount of authority<sup>85</sup> the board of directors and consequently majority shareholders should have. Examples involving decisions considered at Yukos and Rosneft's general meetings reveal the extent of authority desired by the management. Perhaps Yukos' example is the most extreme when the board of directors asked shareholders to grant them authority to issue new shares without approval of the latter. Although this resolution was voted down, it nevertheless exposed the level of alertness required from minority investors. On a practical level however, it is evident that general meetings were a weak form of protection because of secret collusions and subtle stealth that could lead to approval of the most daring proposals (Rosneft). The second scenario

<sup>85</sup> Hence control is a strongly represented second order code.



extracted from the reported material refers to situations when general meetings were treated as a formality with the actual decision being made behind closed doors. The key point here is that in some cases approval of shareholders was not even considered as necessary since they were simply prevented from voting on either minor technicalities (Surgutneftegaz, Inkombank) or by physical removal from the venue (Knauf).

In 2006 there were only three disputes featuring general meetings. Those disputes were coded together with misimplementation, diversion of assets and claims categories. This is a visible reduction in reported material directly associated with general meetings. Further details of this category are presented in graph 4.21 and table 4.8.

Graph 4.21: *General Meetings, 2006*

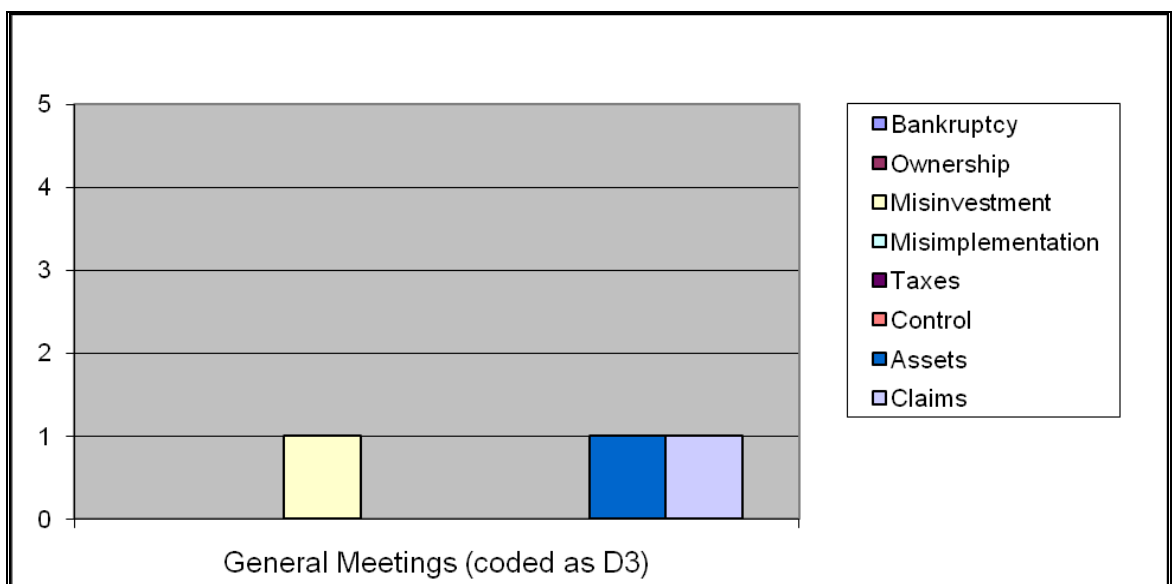


Table 4.8: *General Meetings, 2006*

<b>Company</b>	<b>Issue (decision for approval)</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>		
<b>VimpelCom</b>  <i>1 Article, ref. 4</i> <i>Coding: Misinvestment</i>	Acquisition	Telenor executives accused VimpelCom of convening an illegal extraordinary shareholders meeting and providing misleading information to shareholders regarding VimpelCom's purchase of Ukrainian RadioSystems for \$231.3 million. Both shareholders of VimpelCom have a blocking stake. One of them was interested in a purchase of a competitor of the other. The Russian shareholder provided misleading information at the disputed extra-ordinary shareholders meeting and got the vote its way.
<b>Yukos</b>  <i>1 Article, ref. 12.5</i> <i>Coding: Diversion of Assets</i>	Dismissal of two managers who were accused of trying to hide the company's assets.	The decision to get rid of the two Yukos managers (Bruce Misamore and David Godfrey) was made by the court appointed Yukos receiver (Eduard Rebgun) and enforced by means of an extraordinary shareholder meeting that was ruled to be legitimate by a Dutch court <sup>86</sup> . The two managers were accused of trying to hide the company's assets.
<b>LUKoil</b>  <i>2 Articles, ref. 17.2</i> <i>Coding: Diversion of Claims</i>	Valuation of target companies.	A minority shareholder (Prosperity Capital Management) sought to boost its stake in the subsidiary Ritek (one of LUKoil's production units) to 25% in order to be in a position to block the merger at the upcoming general meeting. The fund offered a 17% premium to other minority shareholders.

In 2006 there was only one dispute that revealed a questionable conduct at a general meeting of shareholders (VimpelCom). Telenor (significant, but minority

<sup>86</sup> A shareholder meeting (which was acknowledged by a Dutch court as legitimate) authorised the decision of the Yukos receiver to fire managers accused of hiding assets in a complex web of transactions.

shareholder) received inaccurate information about a proposed acquisition and was simply tricked into voting in favour of what turned out to be a potentially damaging resolution. Conversely, the dispute involving LUKoil showed that some shareholders began treating general meetings as a reliable mechanism for controlling corporate decisions.

### 3.1.3.1 Implications for the Rule of Law with Reference to General Meetings Disputes

Unlike previous categories, analysis of disputes involving general meeting proceedings exposes a considerable improvement in investor perception of the rule of law in the country. On the surface this conclusion is supported by a significant drop in the number of reported disputes featuring general meetings (11 in 1998 and only 3 in 2006). Furthermore, in terms of the actual content of reported disputes, the blatant abuses of (shareholder) voting rights and illegal resolutions appear to be perceived as a legacy of the past.

Disputes reported in 2006 were fundamentally different in terms of the analysed category. The case involving VimpelCom (2006) was not as straightforward as disputes reported in 1998. Here, a shareholder (Alfa Group) proposed an acquisition of a competitor of the other shareholder (Telenor). Arguably, as far as the company and other minority shareholders were concerned that was a reasonable proposition that happened to be at odds with independent interests of Telenor. Of course it was no justification for withholding or misrepresenting relevant information<sup>87</sup>, but nevertheless the decision at hand probably made economic sense for the entity in question. This is in stark contrast to some of the completely self-centred decisions pushed through at the general meetings reported in 1998. Moreover, in relation to the dispute involving LUKoil the 17% premium on shares paid by a minority shareholder wishing to boost their holding to a blocking stake was a demonstration of the confidence in the legitimacy of the voting process. Such confidence simply did not exist in 1998.

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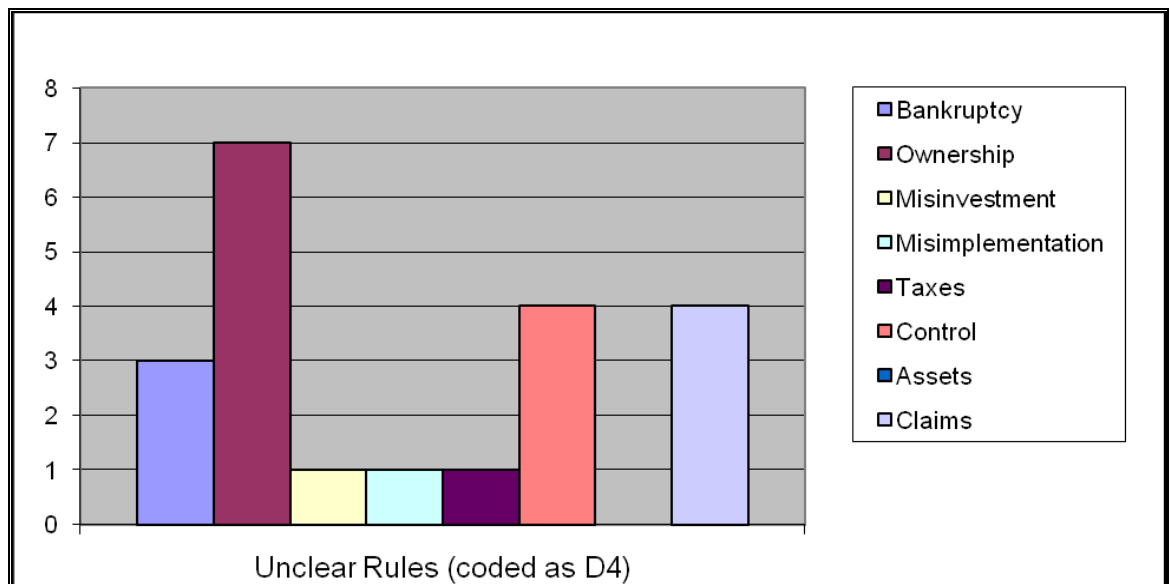
<sup>87</sup> Unfortunately, this characteristic remained an aspect of the perceived environment.

### 3.1.4 Unclear Rules, Laws, Regulations

This category refers to contradictory laws, regulations and court rulings as well as unfulfilled contracts and corporate obligations that cause confusion among affected parties. Such contradictions can arise as a result of directly conflicting pieces of legislation as well as inadequate arbitration. This category serves as an indication of the perceived level of ambiguity within the primarily external environment.

In 1998 there were 21 disputes<sup>88</sup> involving elements of regulatory contradiction with varying degrees of severity. The largest number of such disputes was associated with the second order code of ownership followed by control and diversion of claims disputes. Conversely to previous categories, a number of bankruptcy disputes also coincided with a great deal of regulatory ambiguity within the environment. Graph 4.22 and table 4.9 provide an overview and content of the reported material corresponding to this category.

Graph 4.22: *Unclear Rules, Laws and Regulations, 1998*



<sup>88</sup> 18 individual disputes of which 3 were parallel coded.

Table 4.9: *Unclear Rules, Laws and Regulations, 1998*

Company	Source of Contradiction	Comments
<i>Template Details Appendix 9a</i>		
<p><b>MGTS</b></p> <p><i>4 articles, ref. 3 Coding: Diversion of Claims</i></p>	<p>Conflict between Joint Stock Company Law and Investor Tender Agreement supported by presidential decree 1210.</p>	<p>The Joint Stock Company Law (1996) prescribed the right of first refusal, whereas the investor tender agreement permitted the majority shareholder to issue new shares and buy them at par value. A presidential decree<sup>89</sup> ruled in favour of the investor tender agreement.</p>
<p><b>GAZ</b></p> <p><i>1 Article, ref. 7 Coding: Taxes</i></p>	<p>Conflict between a presidential decree granting a series of tax breaks and existing tax legislation together with the requirements of the International Monetary Fund.</p>	<p>The International Monetary Fund's opposition forced Russian authorities to scale back on the tax incentives breaking the formal promise to the venture.</p>
<p><b>Gazprom</b></p> <p><i>1 Article, ref. 11.1 Coding: Ownership</i></p>	<p>Despite a ban (presidential decree) on foreign ownership of Gazprom's shares, there were various schemes designed to circumvent the rule.</p>	<p>Regent Fund Management Limited set up a Cayman Islands-based entity called Regent GAZ, which announced plans to buy \$200 million worth of domestic Gazprom shares and sell derivatives to foreign investors avoiding not only the decree, but also local taxes.</p>
<p><b>Yukos</b></p> <p><i>2 Articles, ref. 12.5 Coding: Ownership</i></p>	<p>Yukos broke an earlier signed agreement with Amoco to jointly develop an oil field.</p>	<p>Yukos and Amoco signed an agreement to develop an oil field in 1993 and together won a tender to secure development rights. Amoco invested more than \$100 million in preliminary development of the field. Yukos, however, surprised the oil community when it stated it had "no business relationship" with Amoco.</p>

<sup>89</sup> The presidential decree 1210 ruled in favour of the 1995 investor tender agreement even though it was in breach of the JSC law governing new share emissions. Analysts suggested that Yeltsin issued the decree because of his connection to Luzhkov, the majority shareholder. The investor-tender agreement did not appear in the investment prospectus.

<b>Company</b>	<b>Source of Contradiction</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>		
<b>Transneft</b>  <i>7 Articles, ref. 18 Coding: Diversion of Claims</i>	<p>The Moscow Arbitration Court returned two conflicting rulings with reference to the legitimacy of a share issue.</p>	<p>Before the Finance Ministry annulled the share issue, Transneft's management tried to fight the share dilution in courts. The Moscow Arbitration Court however returned two conflicting verdicts which left two groups of investors claiming control over the company.</p>
<b>UES</b>  <i>8 Articles, ref. 25.4 Coding: Ownership</i>	<p>A bill restricted foreign ownership in the company below existing at the time level.</p>	<p>The State Duma, passed a bill restricting foreign ownership of UES to 25%. The issue was complicated as at the time foreigners had already purchased around 30% of the company. The mechanism for buying back the 5% was unclear<sup>90</sup>.</p>
<b>Electrosila</b>  <i>1 Article, ref. 27 Coding: Control</i>	<p>Majority shareholder ignored decision of the Moscow Arbitration Court to reinstate a fired director.</p>	<p>When the director was replaced, Siemens took the case to court and received a ruling in its favour (the decision to replace the director was in violation of the company's charter). EMK, majority shareholder in Elektrosila, ignored the decision and installed a new director who was working alongside the old one. Most analysts suggested that Siemens would lose because EMK was a majority shareholder and a powerful corporation.</p>
<b>Novolipetsk</b>  <i>4 Articles, ref. 29.1 Coding: Control</i>	<p>There were a number of conflicting decisions that the Lipetsk arbitration court returned.</p>	<p>A 40 percent minority was blocked from getting a fair board representation.</p>

<sup>90</sup> The Russian Constitution explicitly forbids expropriation of property, but the state could not afford the \$600 million it would have cost to buy back the 5 percent of the foreign-owned stock.

Company	Source of Contradiction	Comments
<i>Template Details Appendix 9a</i>		
<b>Magnitogorsk</b>  <i>3 Articles: ref. 33 Coding: Ownership</i>	A renegade <sup>91</sup> director was reinstated by a Moscow district court even though he was accused of direct insubordination.	A company that managed shares of Magnitogorsk refused to hand in the shares that were meant to be used as collateral for a loan from the EBRD. The director of the company that hid the shares was sacked but later reinstated by a court leading to the two parties to the conflict holding their own board meetings.
<b>Lebedinsky Ore Mining Plant</b>  <i>2 Articles, ref. 34 Coding: Ownership</i>	Russian courts returned a number of contradictory rulings with regard to the ownership of the government's stake in the plant.	The disputed stake went through a series of transactions, which the courts tried to unravel. Eventually, the court system came up with two contradictory rulings complicating the situation <sup>92</sup> . Finally, the government suggested that although the ultimate stock holder obtained the shares legitimately, it was not theirs as in the past the disputed stock was sold improperly.
<b>Achinsk Alumina Combine</b>  <i>1 Article, ref. 35 Coding: Bankruptcy/ Misinvestment/ Control</i>	A higher-order court accepted an appeal and sent the case back to Kransoyarsk arbitration court for another hearing.	The creditors (including Alfa Groups) were pressing for bankruptcy while regional administration argued that the bankruptcy would be disastrous for the region. The conflicting decisions of the courts appeared to be consistent with the change of heart of the Governor Lebed who suddenly withdrew his support for the creditors.

<sup>91</sup> A renegade director is someone who refuses to accept or openly challenges authority of rightful owners.

<sup>92</sup> An arbitration court cancelled the sale soon after, ruling that it constituted insider trading. However, the Belgorod regional court, a higher authority, said the sale could go ahead.

<b>Company</b>	<b>Source of Contradiction</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>		
<b>AssiDoman</b>  <i>6 Articles, ref. 38.2 Coding: Ownership</i>	<p>The State Anti-Trust Committee sold a stake in a paper mill to AssiDoman. The Moscow Arbitration Court declared the sale illegal.</p>	<p>Legality of the purchase was questioned because allegedly someone else became interested in the stake. The courts were used to challenge the legitimacy of the stake. Subsequently, AssiDoman expressed a wish to sell its stake saying that it had underestimated problems with Russian bureaucracy.</p>
<b>SBS Agro</b>  <i>5 Articles, ref. 40.2 Coding: Bankruptcy</i>	<p>Sberbank promised to repay SBS Agro's clients, but later retracted its offer.</p>	<p>Although the Central Bank had said SBS-Agro depositors could have access to their funds, it later retracted that pledge. At some point due to lack of cash, the bank decided to pay depositors on the basis of their needs. This was an arbitrary approach open to abuse.</p>
<b>EBRD</b>  <i>1 Article, ref. 45 Coding: Bankruptcy</i>	<p>The put option designed under the British law was not recognised by the Russian law.</p>	<p>The put option would have allowed the EBRD to sell back a stake in Tokobank. The option was not recognised by the Russian law (equal treatment of all shareholders) in the face of bankruptcy proceedings. The EBRD accepted the loss of the stake and wrote off its investment.</p>
<b>Tokobank</b>  <i>1 Article, ref. 46 Coding: Diversion of Claims</i>	<p>Futures contracts.</p>	<p>Tokobank used a loophole in the Russian law to avoid settling futures contracts which became highly unprofitable as a result of the devaluation of the ruble. Currency forward contracts were treated as wagers and according to the Russian civil code wagers could not be settled by a court unless one of the sides was coerced or deceived into making the bet.</p>



<b>Company</b>	<b>Source of Contradiction</b>	<b>Comments</b>
<i>Template Details Appendix 9a</i>		
<b>Rossiisky Kredit</b>  1 Article, <i>ref. 47</i> <i>Coding: Diversion of Claims</i>	Conflict between a court order and actions of the tax authorities	The bank (Rossiisky Kredit) refused to transfer its client's deposit meant for wages and taxes. The court ruled in favour of the client and bailiffs seized the property of the bank. However, the bank argued that the transaction was declined because the tax authorities had frozen the account of the client. The bank appealed the decision.
<b>Kosmos TV</b>  1 Article, <i>ref. 49</i> <i>Coding: Control</i>	Conflict between the Joint Stock Company Law and the Labour Code	A renegade director took the shareholders of Kosmos TV to court over his dismissal. In the 1990s the Russian courts were much more familiar with the Labour Code than the JSC Law and used the former much more readily. The decision raised concerns since it proved impossible for companies to sack their directors even on legitimate grounds <sup>93</sup> .
<b>Kuznetsky Mine</b>  1 Article, <i>ref. 54</i> <i>Parallel Coding: Ownership/ Misimplementation</i>	An appeals court invalidated the ruling of Kemerovo Arbitration Court	The local court challenged the legitimacy of the mine's privatisation, but the appeals court invalidated the ruling.

In summary, 1998 was a fairly contradictory environment where the same court returned completely opposing rulings (Transneft, Lebedinsky Ore Mining Plant and Novolipetsk), appeals were used to procrastinate and delay verdicts, (Kuznetsky Mine, Rossiisky Kredit and Achinsk Alumina Combine), presidential decrees openly challenged existing legislation (MGTS and GAZ), new pieces of legislation destroyed the status quo (UES) and crucially where there was a complete disregard for the newly enforced Law on Joint Stock Companies (1998). Despite

<sup>93</sup> Foreign investors and the Russian partners respected the decision of the court and were forced to reinstate the renegade director.

being a higher order law it was frequently ignored in favour of the Labour Code which was developed under the Soviet system and enjoyed a greater support from the Russian judiciary (Magnitogorsk, Kosmos TV and MGTS).

In 2006 there were 11<sup>94</sup> disputes pertaining to the category reported in the newspaper. The most significant second order codes here were represented by diversion of claims and ownership conflicts.

Graph 4.23: *Unclear Rules, Laws and Regulations, 2006*

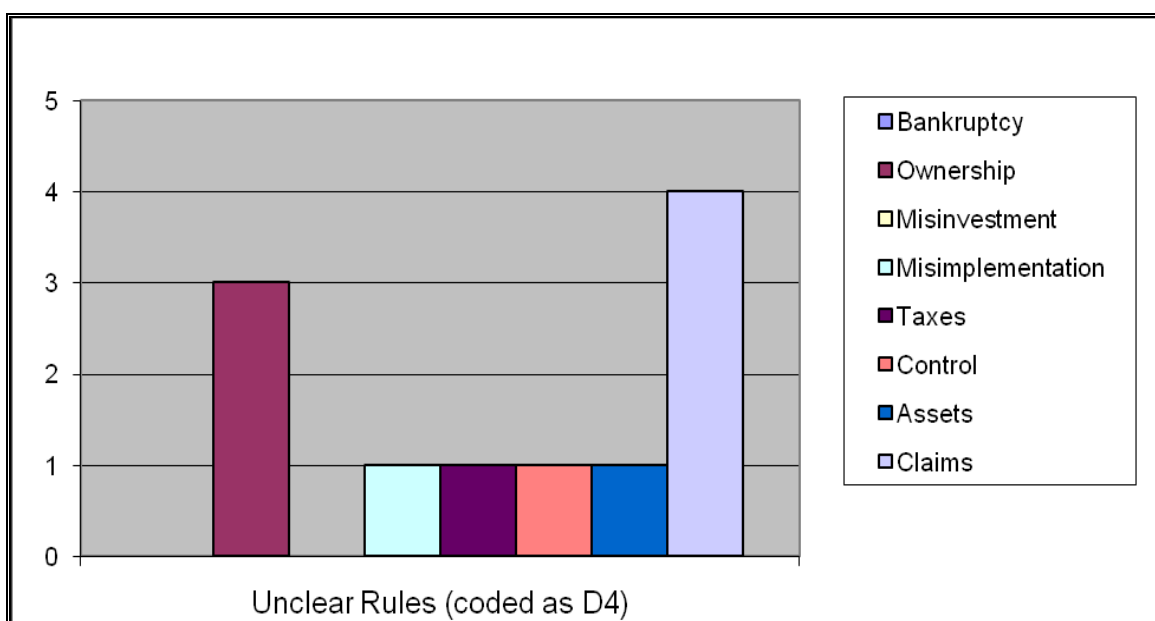


Table 4.10: *Unclear Rules, Laws and Regulations, 2006*

Company	Source of Contradiction	Comments
<i>Template Details Appendix 9b</i>		
<b>AvtoVaz</b> <i>2 Articles, ref. 6</i> <i>Parallel Coding: Control/Taxes</i>	The General Prosecutor's Office cancelled a criminal investigation into AvtoVaz without giving any explanations.	The city of Samara police opened a criminal investigation into unidentified AvtoVAZ employees over the alleged non-payment of 230 million rubles (\$8 million) in back taxes. Allegedly, the charges were dropped because influential stakeholders of AvtoVaz agreed to co-operate with the government.

<sup>94</sup> 7 individual disputes of which 4 were parallel coded.

<b>Company</b>	<b>Source of Contradiction</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>		
<b>Rosneft</b>  <i>3 Articles, ref. 10.2 Coding: Diversion of Claims</i>	Lack of legislation on valuation methods.	Companies are allowed to pick a valuation method. Management of Rosneft used the most favourable one and with the legal profession lacking expertise, accountants had greater freedom to 'massage' the figures.
<b>Gazprom</b>  <i>1 Article, ref. 11.1 Coding: Ownership</i>	Gazprom broke an agreement with Moncrief Oil International to jointly develop a gas field <sup>95</sup> .	According to Gazprom the agreement unambiguously specified that any arising disputes must be settled in the Russian Courts.
<b>Gazprom</b>  <i>4 Articles, ref. 11.3 Parallel Coding: Diversion of Assets/ Ownership</i>	De facto rules were established before the law came out.	The government decided to consolidate control over the oil and gas sector (Gazprom was the main beneficiary of this action), yet systematically delayed the law on strategic assets.
<b>Gazprom</b>  <i>4 Articles, ref. 11.5 Parallel Coding: Diversion of Claims/Ownership</i>	Failure to honour a supply contract.	Gazprom suddenly moved to breach a five-year contract signed with Ukraine in August 2004 that set the gas price at \$50 pcm. The move was hailed as politically motivated.
<b>Yukos</b>  <i>1 Article, ref. 12.3 Coding: Diversion of Claims</i>	Insider dealing was not a crime under Russian law.	Gazprombank executives used insider information when they sold Yukos shares short one day before a Russian court upheld a back-tax bill of \$3.5 billion against the company.

<sup>95</sup> Moncrief Oil International wanted to sue BASF over its involvement in Gazprom's vast Yuzno-Russkoye gas field. In the 1990s there was an agreement that Moncrief would take 40% in the field but instead Gazprom swapped assets with BASF.

Company	Source of Contradiction	Comments
<i>Template Details Appendix 9b</i>		
<b>IKEA</b>  <i>4 Articles, ref. 48</i> <i>Parallel Coding: Misimplementation/ Diversion of Claims</i>	The fire code was very vague and open to different interpretations.	An IKEA owned shopping complex was closed by a local court for fire violations <sup>96</sup> . The closure coincided with the busy Christmas period and may have been linked to an unidentified business group that allegedly benefited from the closure.

The most recent year of the investigation reveals a number of sources of ambiguity related to the above-mentioned category. With the corporate governance reform going strong for some time and large Russian corporations preparing for international Initial Public Offerings it was extremely surprising to see insider dealing as a legal activity in Russia in 2006 (Yukos). This is particularly confusing in the Russian context where ubiquitous political and corporate cronyism was a key concern among legislators and investor analysts. Vague rules (IKEA), controlled regulatory pressure (AvtoVAZ, Gazprom) and broken contractual obligations (Gazprom) continue to be a feature of the Russian environment firmly set in the minds of foreign investors.

#### 3.1.4.1 Implications for the Rule of Law with Reference to Unclear Rules, Laws and Regulations Disputes

Comparison of the reported disputes pertaining to the two years of the investigation reveals a moderate improvement in the environment with reference to a perceived level of regulatory ambiguity. First, the number of instances featuring this category fell by 10 entries in the more recent year of the study. Moreover, 2006 was largely free from crude forms of regulatory contradiction

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<sup>96</sup> An inspection commission accused the mall of 887 fire-code violations. The company corrected 214 violations but another 22 were discovered. A final inspection revealed that 741 fire code violations remained uncorrected.

stemming from conflicting laws and presidential decrees. However, a degree of caution must be expressed with regard to this proposition because in 2006 there were still plenty of peripheral laws that allowed arbitrary interpretation making corporate raids possible from the legislative perspective (e.g. fire code and environmental legislation). Additionally, emergence of unwritten rules generated a great deal of negative publicity. In an unambiguous environment formal rules determine practice. But in the instance of the Russian government's drive to renationalise key strategic assets, practice preceded the rules. Partially, it is for this reason that foreign investors have a strong impression that in 2006 the Russian government was above the law in the country.

### 3.1.5 Transactions with Self-Interest

This category views corporate disputes from the perspective of interested parties. It includes practices such as transfer pricing, insider dealing, assets stripping, appraisal of assets and share dilution. However, the main focus of the analysis is on the alleged identity of benefiting parties. Here association with second order codes demonstrates whether such self-centred actions were limited to a straightforward diversion of funds or, in more extreme cases, led to noticeable changes in ownership structure and levels of control.

In 1998 there were 55 disputes<sup>97</sup> with elements of the above category. This is the biggest third order code in the study. It is not surprising since very often corporate conflicts are fuelled by self-centred actions of the stakeholders involved<sup>98</sup>. In 1998 a vast majority of reported disputes were under the hierarchy of the diversion of claims code. However, control and ownership codes were also visibly represented in the graphical representation of the reported material (see graph 4.24 and table 4.11).

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<sup>97</sup> 43 individual disputes of which 12 were parallel coded.

<sup>98</sup> Agency theory

Graph 4.24: Transactions with Self-Interest Disputes, 1998

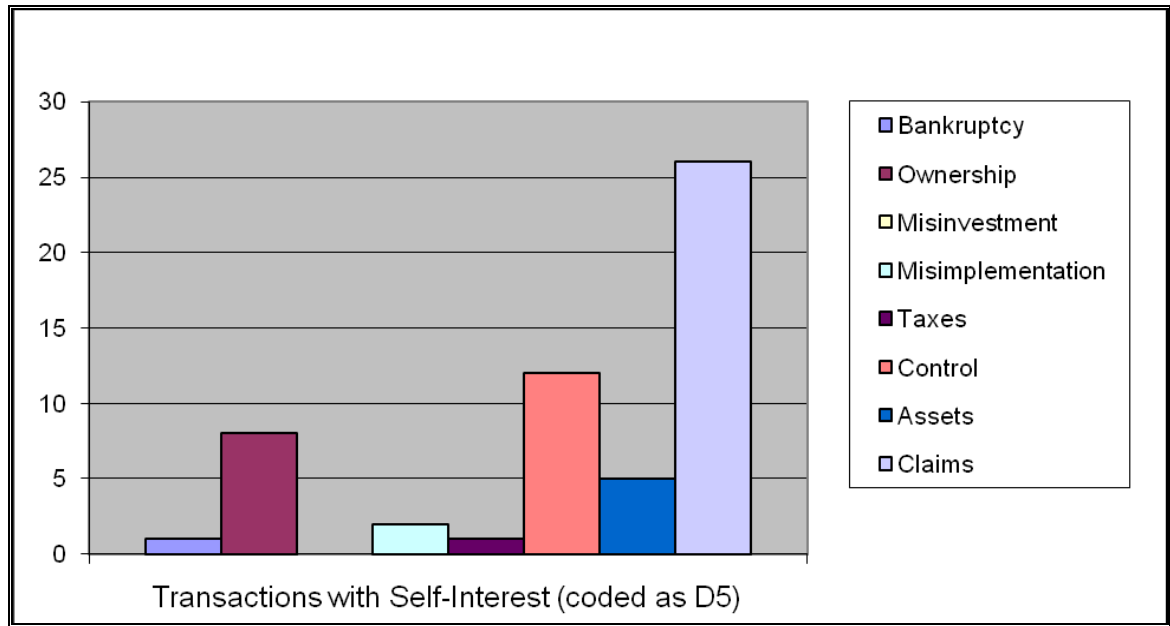


Table 4.11: Transactions with Self-Interest Dispute, 1998

Company	Benefiting Party	Nature of the Transactions
<i>Template Details Appendix 9a</i>		
<b>Aeroflot</b> <i>1 Article, ref. 1 Coding: Diversion of Claims</i>	Majority shareholder (Boris Berezovsky)	Insider dealing
<b>MGTS</b> <i>4 Articles, ref. 3 Coding: Diversion of Claims</i>	AO Sistema (a secretive outfit with links to Yury Luzhkov)	Share dilution
<b>VimpelCom</b> <i>2 Articles, ref. 4 Coding: Control</i>	First Deputy Prime Minister Yury Maslyukov	Insider dealing
<b>AvtoVaz</b> <i>1 Article, ref. 6 Coding: Diversion of Claims</i>	Criminal dealerships	Insider dealing
<b>KamAz</b> <i>2 Articles, ref. 8 Coding: Diversion of Claims</i>	Majority shareholders	Share dilution

<b>Company</b>	<b>Benefiting Party</b>	<b>Nature of the Transactions</b>
<i>Template Details Appendix 9a</i>		
<b>Rosneft</b> <i>8 Articles, ref. 10.1 Coding: Diversion of Assets</i>	Creditors and unidentified buyers	Appraisal of assets
<b>Rosneft</b> <i>2 Articles, ref. 10.2 Coding: Diversion of Claims</i>	Managers of Purneftegaz and Sibneft's shareholders (allegedly Berezovsky)	Transfer pricing
<b>Gazprom</b> <i>1 Article, ref. 11.6 Coding: Diversion of Assets</i>	Gazprom managers	Appraisal of assets
<b>Gazprom</b> <i>1 Article, ref. 11. 7 Diversion of Claims</i>	Management of Gazprom	Insider dealing
<b>Yukos</b> <i>10 Articles, ref. 12.1 Parallel Coding: Diversion of Claims/Control</i>	Majority shareholder (Khodorkovsky)	Transfer pricing
<b>Yukos</b> <i>1 Article, ref. 12.2 Coding: Diversion of Claims</i>	Directors of Yukos	Share dilution
<b>Yukos</b> <i>1 Article, ref. 12.3 Coding: Diversion of Claims</i>	Majority shareholder (Khodorkovsky)	Asset stripping
<b>Yukos</b> <i>1 Article, ref. 12.4 Coding: Diversion of Claims</i>	Majority shareholder (Khodorkovsky)	Asset stripping
<b>Yukos</b> <i>1 Article, ref.12.9 Coding: Diversion of Claims</i>	Menatep Group	Share dilution

<b>Company</b>	<b>Benefiting Party</b>	<b>Nature of the Transactions</b>
<i>Template Details Appendix 9a</i>		
<b>Transneft</b> <i>7 Articles, ref. 18 Coding: Diversion of Claims</i>	Former president of Transneft and several of his deputies.	Appraisal of assets
<b>Surgutneftegaz</b> <i>2 Articles, ref. 19 Coding: Diversion of Claims</i>	St. Petersburg administration and local criminal underworld.	Transfer pricing
<b>Sibneft</b> <i>1 Article, ref. 21.1 Coding: Control</i>	Majority shareholder (allegedly Berezovsky).	Transfer pricing and insider dealing
<b>Sibneft</b> <i>5 Articles, ref. 21.2 Parallel Coding: Diversion of Claims/Diversion of Assets</i>	Majority shareholder (allegedly Berezovsky).	Transfer pricing and share dilution
<b>Sidanko</b> <i>6 Articles, ref. 22.1 Coding: Diversion of Claims</i>	Majority shareholder (Potanin)	Share dilution
<b>Sidanko</b> <i>2 Articles, ref. 22.4 Coding: Bankruptcy</i>	Majority shareholder (Potanin)	Transfer pricing
<b>Tyumen</b> <i>7 Articles, ref. 23 Coding: Control</i>	Alfa Group (Mikhail Fridman)	Appraisal of assets
<b>Krasnoyarsk Hydro Plant</b> <i>4 Articles, ref. 24 Parallel Coding: Control/ Diversion of Claims</i>	Financial Industrial Group Tanako	Appraisal of assets



<b>Company</b>	<b>Benefiting Party</b>	<b>Nature of the Transactions</b>
<i>Template Details Appendix 9a</i>		
<b>UES</b> <i>11 Articles, ref. 25.1 Coding: Control</i>	Chairman of UES (Dyakov)	Transfer pricing and insider dealing
<b>UES</b> <i>4 Articles, ref. 25.2 Coding: Control</i>	Chubais (a well connected politician and one of the contenders for the CEO position).	Insider dealing
<b>Mosenergo</b> <i>1 Article, ref. 26 Coding: Diversion of Claims</i>	Majority shareholders	Share dilution
<b>Norilsk Nickel</b> <i>1 Article, ref. 28.1 Coding: Diversion of Claims</i>	Majority shareholder (Potanin).	Appraisal of assets
<b>Norilsk Nickel</b> <i>1 Article, ref. 28.2 Coding: Ownership</i>	Ordinary shareholders	Share dilution
<b>Novolipetsk</b> <i>3 Articles, ref. 29.2 Parallel Coding: Diversion of Claims/Control</i>	Trans-World Group.	Transfer pricing
<b>Magnitogorsk</b> <i>3 Articles, ref. 33 Coding: Ownership</i>	Sharipov (CEO of a company that was charged with the task of managing a 25% stake).	Asset stripping
<b>Lebedinsky Ore Mining Plant</b> <i>2 Articles, ref. 34.1 Coding: Ownership</i>	ZAO RudementInvest	Insider dealing

<b>Company</b>	<b>Benefiting Party</b>	<b>Nature of the Transactions</b>
<i>Template Details Appendix 9a</i>		
<b>Lebedinsky Ore Mining Plant</b>  <i>1 Article, ref. 34.2 Coding: Diversion of Claims</i>	Majority shareholder and management	Share dilution
<b>Knauf</b>  <i>1 Article, ref. 36.1 Parallel Coding: Control/Ownership</i>	Director of joint venture Kubansky Gips-Knauf (Alim Sergiyenko).	Share dilution
<b>Knauf</b>  <i>1 Article, ref, 36.2 Parallel Coding: Taxes/Control</i>	Tax police and an unidentified third party.	Asset stripping
<b>MOST Bank</b>  <i>1 Article, ref. 43 Parallel Coding: Misimplementation/ Diversion of Claims</i>	Uneximbank's officials.	Insider dealing
<b>Pioneer Group</b>  <i>1 Article, ref. 44 Coding: Diversion of Claims</i>	Pioneer Bank officials.	Insider dealing
<b>Channel 5</b>  <i>1 Article, ref. 50 Diversion of Claims</i>	Advertising companies Premier SV and LISS owned by Lisovsky (close ally of Berezovsky).	Assets stripping and transfer pricing
<b>ORT</b>  <i>1 Article, ref. 51.1 Coding: Diversion of Claims</i>	Yeltsin, Beresovsky, Korzhakov.	Insider dealing
<b>Subway</b>  <i>7 Articles, ref. 52 Parallel Coding: Control/Diversion of Assets/Ownership</i>	A renegade director of the joint venture (Bordug).	Insider dealing

<b>Company</b>	<b>Benefiting Party</b>	<b>Nature of the Transactions</b>
<i>Template Details Appendix 9a</i>		
<b>Lomonosov Porcelain Factory</b>  <i>1 Article, ref. 53 Coding: Ownership</i>	Brokerages and criminal circles.	Appraisal of assets
<b>Kuznetsky Mine</b>  <i>1 Article, ref. 54 Parallel Coding: Ownership/ Misimplementation</i>	Kemerovo administration.	Appraisal of assets
<b>MCCI</b>  <i>1 Article, ref. 55 Parallel Coding: Control/ Diversion of Assets/ Ownership</i>	A state owned company GlavUpDK.	Insider dealing
<b>Standard MNT</b>  <i>1 Article, ref. 56 Coding: Diversion of Claims</i>	A police department in St. Petersburg.	Assets stripping
<b>Post Office</b>  <i>1 Article, ref. 57 Coding: Diversion of Claims</i>	The Russian Post Office and key bureaucrats close to the company.	Transfer pricing, insider dealing

*Below is the summary of various forms of transactions reported in 1998:*

Type of transaction	Companies
Insider Dealing	Aeroflot, VimpelCom, AvtoVaz, Gazprom, Sibneft, UES, UES, Lebedinsky Ore Mining Plant, MOST Bank, Pioneer Group, ORT, Subway, MCCI, Post Office (14 disputes).
Appraisal of Assets	Rosneft, Gazprom, Transneft, Tyumen, Krasnoyarsk Hydro Plant, Norilsk Nickel, Lomonosov Porcelain Factory, Kuznetsky Mine (8 disputes).
Asset Stripping	Yukos, Yukos, Magnitogorsk, Knauf, Channel 5, Standart NMT (6 disputes).
Transfer Pricing	Rosneft, Yukos, Surgutneftegaz, Sibneft, Sibneft, Sidanko, UES, Novolipetsk, Channel 5, Post Office (10 disputes).
Share Dilution	MGTS, KamAz, Yukos, Yukos, Sidanko, Mosenergo, Norilsk Nickel, Lebedinsky Ore Mining Plant, Knauf (9 disputes).

In summary, 1998 involved a variety of stakeholder groups who allegedly abused the corporate system to their advantage. On the government's side there were examples of when Boris Yeltsin allegedly received a large number of shares in ORT as a bribe from the then financial tycoon Boris Berezovsky and Anatoly Chubais (Chief Executive of UES) who allegedly walked out of the Russian white house with a \$90 thousand dollar bribe for fixing a privatisation deal<sup>99</sup>. On the local administration level, there was a case involving Surgutneftegaz when subsidiaries diluted the stake of the parent to almost nothing with the help of St. Petersburg officials. Additionally, there were a lot of transactions to the benefit of well-connected individuals like Khodorkovsky, Berezovsky, Potanin, Fridman on the

<sup>99</sup> Interestingly, Chubais sued an investigative journalist and a radio station for libel at the time of the alleged offence when the journalist openly accused him of accepting the bribe. Although Chubais was never convicted, a Moscow district court ruled in favour of the journalist and did not award any damages.

oligarchic level and Bordug, Lisovsky, Sharipov and Sergiyenko on a more modest level of private 'entrepreneurs'.

In 2006 a vast majority of disputes associated with transactions with self-interest were also connected with the diversion of claims code. In total there were 31 disputes<sup>100</sup> with only a single category of misinvestment not represented in the hierarchy of codes.

Graph 4.25: *Transactions with Self-Interest Disputes, 2006*

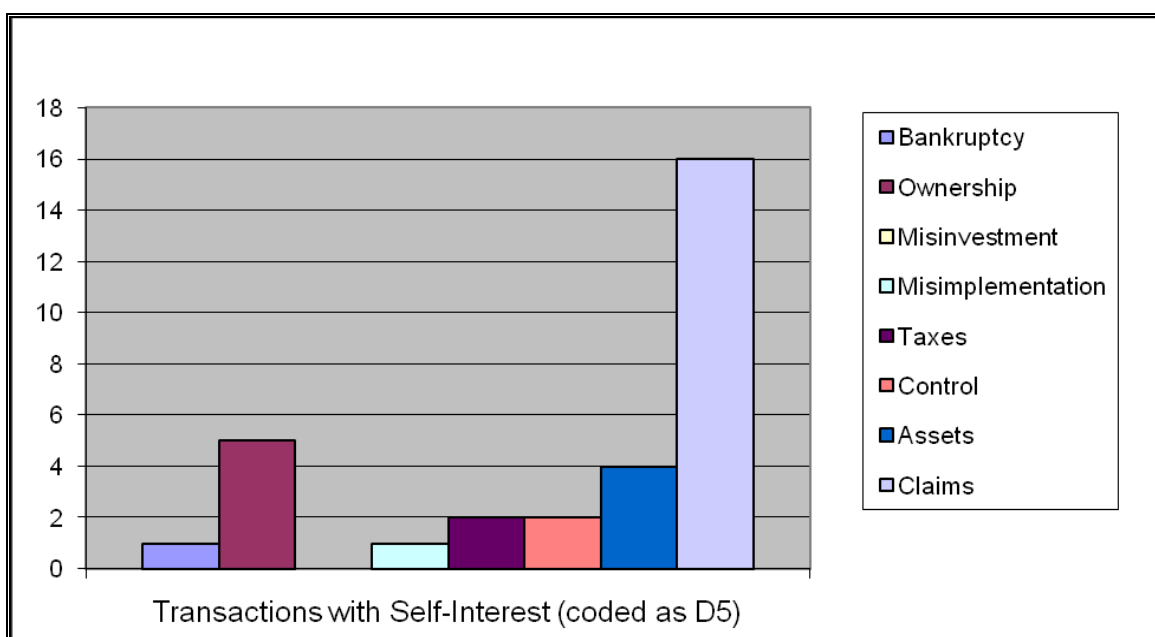


Table 4.12: *Transactions with Self-Interest Disputes, 2006*

Company	Benefiting Party	Comments
<i>Template Details Appendix 9b</i>		
<b>MegaFon</b> <i>2 Articles, ref. 5 Parallel Coding: Diversion of Assets/ Control</i>	IT and Telecommunications minister Leonid Reiman	Share dilution
<b>Rosneft</b> <i>1 Article, ref. 10.1 Coding: Diversion of Claims</i>	Unidentified government and Rosneft officials.	Insider dealing

<sup>100</sup> 21 individual disputes of which 10 were parallel coded.

<b>Company</b>	<b>Benefiting Party</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>		
<b>Rosneft</b>  <i>3 Articles, ref. 10.2 Coding: Diversion of Claims</i>	Majority shareholder (the Russian state)	Appraisal of Assets
<b>Rosneft</b>  <i>1 Article, ref. 10.3 Parallel Coding: Diversion of Assets/ Diversion of Claims</i>	Majority shareholders of Rosneft (Russian government).	Transfer pricing
<b>Rosneft</b>  <i>6 Articles, ref. 10.5 Parallel Coding: Diversion of Assets/ Diversion of Claims</i>	Majority shareholders of Rosneft (Russian government).	Appraisal of Assets
<b>Gazprom</b>  <i>1 Article, ref. 11.2 Parallel Coding: Diversion of Assets/ Diversion of Claims</i>	Management of Gazprom and Itera.	Asset stripping
<b>Gazprom</b>  <i>4 Articles, ref. 11.5 Parallel Coding: Diversion of Claims/ Control</i>	Russian politicians and secret owners of RosUkrEnergo.	Insider dealing
<b>Yukos</b>  <i>23 Articles, ref. 12.1 Parallel Coding: Ownership/Control/Taxes</i>	Rosneft and the government	Asset stripping
<b>Yukos</b>  <i>2 Articles, ref. 12.2 Coding: Diversion of Claims</i>	Rosneft and the government	Asset stripping
<b>Yukos</b>  <i>1 Article, ref. 12.3 Coding: Diversion of Claims</i>	Gazprombank executives	Insider dealing

<b>Company</b>	<b>Benefiting Party</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>		
<b>Yukos</b>  <i>8 Articles, ref. 12.4 Coding: Bankruptcy</i>	The government	Insider dealing
<b>Yukos</b>  <i>6 Articles, ref. 12.6 Coding: Diversion of Assets</i>	Rosneft shareholders (the state)	Appraisal of Assets
<b>Yukos</b>  <i>2 Articles, ref. 12.7 Coding: Control</i>	Unnamed third parties.	Transfer pricing
<b>LUKoil</b>  <i>2 Articles, ref. 17.2 Coding: Diversion of Claims</i>	Majority shareholders of LUKoil	Appraisal of Assets
<b>Novolipetsk</b>  <i>1 Article, ref. 29 Parallel Coding: Diversion of Claims/ Control</i>	The chairman Vladimir Lisin	Transfer pricing
<b>Severstal</b>  <i>2 Articles, ref. 30.1 Parallel Coding: Diversion of Claims/Control</i>	CEO Mordoshov	Transfer pricing
<b>Evrax</b>  <i>1 Article, ref. 31.1 Coding: Taxes</i>	Majority shareholder (Abramovich)	Transfer pricing
<b>RusAl</b>  <i>1 Article, ref. 32.1 Coding: Diversion of Claims</i>	Minority shareholders (Derepaska)	Appraisal of Assets
<b>RusAl</b>  <i>1 Article, ref. 32.2 Coding: Diversion of Claims</i>	RusAl shareholders (Derepaska)	Appraisal of Assets

<b>Company</b>	<b>Benefiting Party</b>	<b>Comments</b>
<i>Template Details Appendix 9b</i>		
<b>Eurocement</b>  <i>1 Article, ref. 37 Coding: Diversion of Claims</i>	Majority owners of Eurocement.	Transfer pricing
<b>IKEA</b>  <i>4 Articles, ref. 48 Parallel Coding: Diversion of Claims/ Misimplementation</i>	An unidentified business group.	Asset stripping

*Below is the summary of various forms of transactions with self-interest reported in 2006:*

<b>Type of transaction</b>	<b>Companies</b>
Insider Dealing	Rosneft, Gazprom, Yukos, Yukos, (4 disputes).
Appraisal of Assets	Rosneft, Rosneft, Yukos, LUKoil, RusAl, RusAl. (6 disputes).
Asset Stripping	Gazprom, Yukos, Yukos, IKEA (4 disputes).
Transfer Pricing	Rosneft, Yukos, Novolipetsk, Severstal, Evraz, Eurocement (6 disputes).
Share Dilution	MagaFon (1 dispute)

The main characteristic in 2006 was a very clear shift away from private individuals benefiting from questionable corporate conduct towards the government. Even disputes involving private individuals like Severstal's Mordoshov and Evraz's Abramovich were all visibly connected to the government's agenda; perhaps with the exception of the cases involving MagaFon's share dilution by the IT and Communications Minister Leonid Reiman, Eurocement's transfer pricing and IKEA's assets stripping. All remaining transactions were conducted to the benefit of the government or were forcefully challenged if they were not in the interests of the latter.



### 3.1.5.1 Implications for the Rule of Law with Reference to Transactions with Self-Interest Disputes

The number of disputes falling into this category fell by 24 in 2006 in comparison with the 1998 data. This fall is a sign of a positive change in perception determined by the reported material. Fewer instances of transactions with self-interest can only be greeted positively by the investment community. In terms of the change in the substance of the reported material, the extent of misappropriation subsided only with regard to private companies such as Severstal, Evraz and RusAl. A vivid example here is what was felt as an inadequate valuation of RusAl's assets. Of course it is possible that the valuation was in fact inadequate, but at the same time outright misappropriation would have been a corporate death for a company preparing for an Initial Public Offering. Similar logic was also applicable to Severstal and Evraz. This trend was not repeated by massive state corporations which continued to be associated with numerous self-centred transactions. The main difference however is that in the 1990s the ultimate beneficiaries of the outright misappropriation were identifiable from reported material, whereas in 2006 the end stakeholders were hidden behind sprawling state-controlled entities.

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## Section 4: Analysis of the Content of the Third Order Codes

In this section, the content of dispute resolution codes is discussed. All of the disputes mentioned here have been referred to previously. However, the emphasis of the analysis is not on the nature of the disputes themselves, but on what the parties do under the circumstances.

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### 4.1 Third Order Codes (Dispute Resolution)

The current theme is designed to depict the process of dispute resolution. In the instance of a conflict of interests (defined by the hierarchy of codes presented at the beginning of this chapter), there could be a variety of strategies employed by the affected parties. In the western context litigation would be the most immediate and understandable example of how parties go about protecting their interests. However, for a variety of reasons previously discussed in the literature review chapter, in the Russian context a number of alternative enforcement strategies need to make up for the deficiency of the legal system<sup>101</sup>. In this section of the analysis, the evolving nature of these strategies is discussed with reference to the collected data and in conjunction with the second order codes. Similar to the previous sections, the analysis focuses on the content of selected codes and seeks to conclude with regard to the implications for the rule of law in the country.

#### 4.1.1 Relationship-Based Resolution

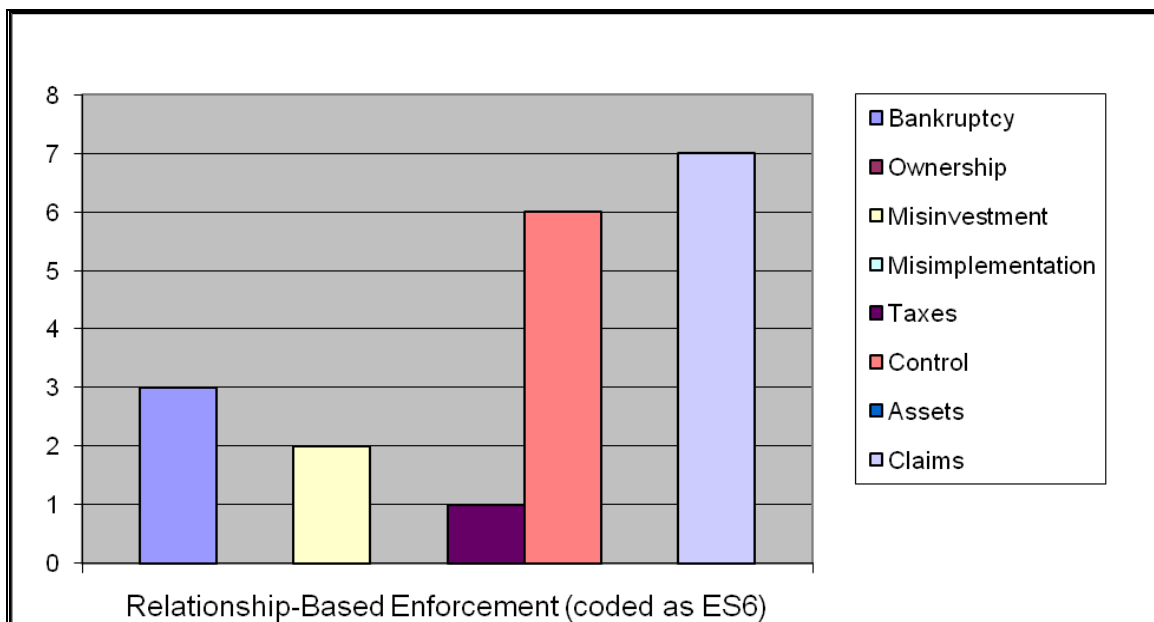
The relationship-based form of dispute resolution refers to situations when affected parties either choose to resolve conflicts by reaching a mutually acceptable agreement, or use personal ties to exploit the situation to their advantage and at the expense of other stakeholders. The latter aspect of the relationship-based resolution seeks to portray the extent of corporate cronyism whereas the former relates to grid-lock situations which can only be resolved by means of a compromise.

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<sup>101</sup> Relationship-based, self, third party, private enforcements as well as administrative levers of the state, shadow of enforcement and litigation.

In 1998 there were 19 disputes<sup>102</sup> with elements of the relationship-based resolution. Below is a graphical representation of the second order disputes reported in 1998 which related to the above category.

Graph 4.26: *Relationship-Based Enforcement, 1998*



In 1998 the following conflicts required a compromise from the affected parties:

Table 4.13: *Relationship-Based Enforcement Involving Compromise, 1998*<sup>103</sup>

Companies	No of Articles	Reference Appendix 9a	Second Order Code
<b>MGTS</b>	<b>4</b>	<i>ref. 3</i>	Diversion of Claims
KamAz	2	<i>ref. 8</i>	Diversion of Claims
Tatneft	1	<i>ref. 20</i>	Bankruptcy
<b>Sidanko</b>	<b>6</b>	<i>ref. 22.1</i>	Diversion of Claims
Sidanko	2	<i>ref. 22.5</i>	Control, Bankruptcy
<b>Tyumen</b>	<b>7</b>	<i>ref. 23</i>	Control

<sup>102</sup> 16 individual disputes of which 3 were parallel coded.

<sup>103</sup> The tables in this section contain company names, number of articles dedicated to a particular dispute, reference to the corresponding template and second order codes. Parallel coding is used when more than one second order code is shown. Entries in bold emphasise disputes that were covered in more than 4 articles.

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Kosmos TV	1 <sup>104</sup>	<i>ref. 49</i>	Control
Channel 5	1	<i>ref. 50</i>	Diversion of Claims

In terms of the conflicts involving MGTS, KamAZ, Tatneft and Sidanko (both disputes) nothing took place, which was somewhat alien to foreign investors. Admittedly, the disputes were indeed serious, but the affected parties needed to reach a workable compromise, sometimes called for by a watchdog (the Federal Securities Commission). Share issues at MGTS and KamAZ, the bond issue and debt restructuring at Sidanko and Tatneft, all involved a compromise that parties to the conflicts could potentially benefit from. A good example here is Tatneft's negotiations with creditors. The company was on the brink of bankruptcy and could not meet its liabilities in a timely fashion. However, from the view point of creditors, a debt restructuring plan was a better option than turning the management of the company against them by demanding immediate payment. The latter approach could increase the risk of receiving nothing. Situations like this required mutually acceptable solutions which in turn favoured a dialogue to unilateral action. However, conflicts involving Tyumen, Kosmos TV and Channel 5 were altogether different. There, an out-of-court settlement appears to have been the ultimate aim of self-centred parties looking for a quick gain. Some businesses were vulnerable to this kind of attack because essentially anybody could challenge property rights and in the 1990s managers (appointed by shareholders) were in the best position to do so.

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<sup>104</sup> This dispute was very extensively reported on in 1997.

Table 4.14: *Corporate Cronyism, 1998*

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Rosneft	2	<i>ref. 10.2</i>	Diversion of Claims
Gazprom	1	<i>ref. 11.7</i>	Diversion of Claims
<b>UES</b>	<b>11</b>	<i>ref. 25.1</i>	Control
<b>UES</b>	<b>4</b>	<i>ref. 25.2</i>	Diversion of Claims
Achinsk Alumina Combine	1	<i>ref. 35</i>	Bankruptcy, Misinvestment and Control
AssiDoman	2	<i>ref. 38.1</i>	Taxes
SBS Agro	1	<i>ref. 40.3</i>	Misinvestment
ORT	1	<i>ref. 51.1</i>	Diversion of Claims

In 1998 a great deal of enforcement power depended upon a close association with key individuals. Managers of Rosneft and Gazprom were able to set up some of the biggest transfer pricing schemes due to their personal affiliation with the right people. Chubais received the CEO job in UES as a result of political bargaining that was only possible if one enjoyed close ties with key individuals in the government. On a local level, the situation was almost identical with bigger deals being arranged only with the informal blessing of governors (Achinsk Alumina Combine). Another example of the role of relationships is Berezovsky's ties with Yeltsin when the former allegedly transferred a large number of shares in ORT to president Yeltsin enabling the tycoon to continue building his unprecedented business portfolio (appendix 9a template 51.1). From this it is possible to determine what kind of perception investors had in terms of the importance of personal connections and affiliations with regard to the business environment in 1998.

In 2006 11 examples<sup>105</sup> of this category were extracted from the Moscow Times reports. Similar to 1998, compromise and corporate cronyism were the themes identified in the reported data.

Graph 4.27: *Relationship-Based Enforcement, 2006*

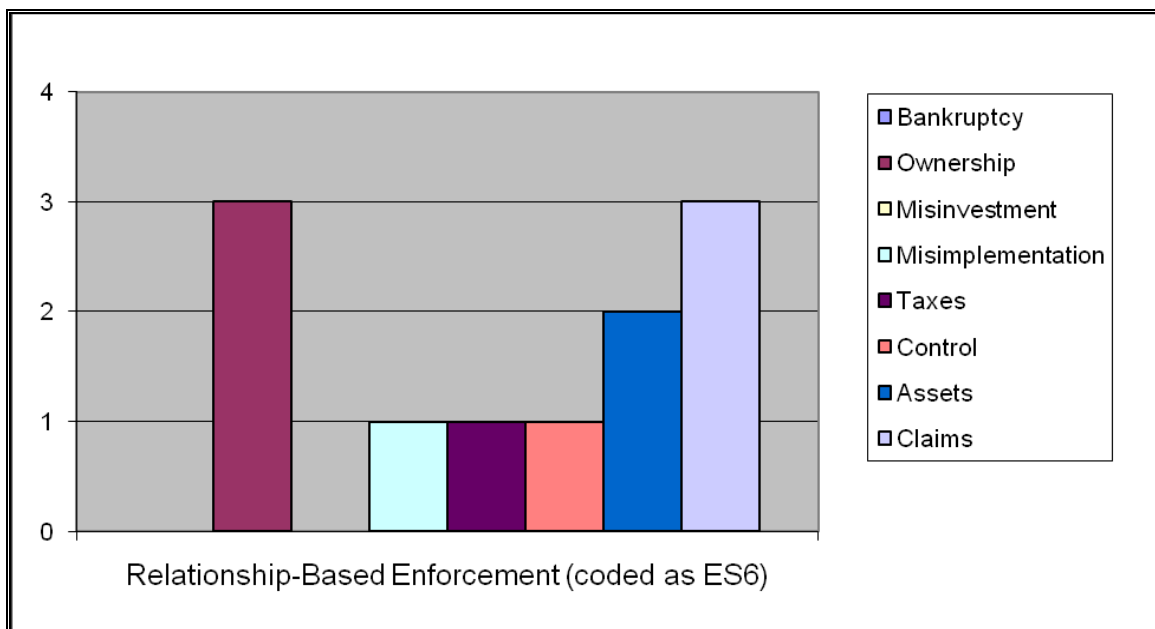


Table 4.15: *Relationship-Based Enforcement Involving Compromise, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
RusAl (template 3)	3	ref. 32.3	Ownership
RusAl (template 4)	1	ref. 32.4	Ownership

Unlike 1998, the more recent year of the study offers only two disputes featuring compromise as a way of resolving conflicts of interests. The first instance related to the disclosure of ownership which meant that previous partners of the ultimate beneficiary had to be silenced by an out-of-court settlement. The second example referred to two oligarchs who had to overcome years of bitter rivalry for the sake of potential benefits from the industry consolidation. Even though this theme was

<sup>105</sup> 8 individual disputes 3 of which were parallel coded.

present in the reports of the newspaper in 2006, the relatively small amount of coverage and fairly non-controversial content rendered compromise less significant in terms of shaping investor perception in the later year of the study.

Table 4.16: *Corporate Cronyism, 2006*

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9b</b>	<b>Second Order Code</b>
<b>Rosneft</b>	<b>6</b>	<i>ref. 10.5</i>	Diversion of Claims, Diversion of Assets
Yukos	2	<i>ref. 12.2</i>	Diversion of Claims
<b>TNK-BP</b>	<b>15</b>	<i>ref. 16.1</i>	Control, Ownership, Diversion of Assets
TNK-BP	1	<i>ref. 16.2</i>	Taxes
<b>Severstal</b>	<b>4</b>	<i>ref. 30.2</i>	Misimplementation
RusAl	1	<i>ref. 32.2</i>	Diversion of Claims

Conversely, corporate cronyism is the category that continued to be visibly represented in the Moscow Times material. Its extent was truly incredible in 2006 with companies like BP trying to get on the right side of the Russian government by opening joint venture discussions with Gazprom and participating in Rosneft's Initial Public Offering. BP officials openly admitted that both were seen as relationship building opportunities aimed at receiving help with licence allocation and not commercial investments. Another vivid example of corporate cronyism transcended national borders when RusAl was accused of conspiring with the president of Nigeria in order to influence the decision in favour of its less attractive bid for Alcon's assets. Finally, connections with high-ranking officials helped to stave off arrest attempts even against a former Yukos employee, Golubovich. Although he was eventually arrested, it did not happen until after president Putin had fired a number of high-ranking FSB<sup>106</sup> officials.

<sup>106</sup> The Federal Security Bureau or FSB is the successor to the Committee of Government Security or KGB.

In comparative terms a positive change must be acknowledged with reference to the forced out-of-court settlements that were frequently reported in 1998 and only once in 2006 (RusAI). However, there appears to be deterioration with reference to the corporate cronyism sub-theme which was elevated to the institutional level in the year 2006. Conversely to 1998 when personal contacts led to favouritism, in 2006 loyalty to the establishment was the perceived key to most valuable assets, licences, permissions and approvals.

#### 4.1.2 Self-Enforcement

The self-enforcement category refers to the situation when parties to the conflict manage to resolve the issue themselves. Although this category could be seen as similar to relationship-based resolution, it is still fundamentally different in that no compromise needs to be reached and unilateral action is a possibility. This category reveals the nature of protective action that stakeholders themselves select to follow without resorting to outside support. Put differently, this method of resolution is about individual action rather than the system.

In 1998 there were 25 examples<sup>107</sup> of self-enforcement with the second order code of diversion of claims most widely represented. Below is the graphical representation of the reported material.

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<sup>107</sup> 22 separate disputes, 3 of which were parallel coded.



Graph 4.28: *Self-Enforcement, 1998*

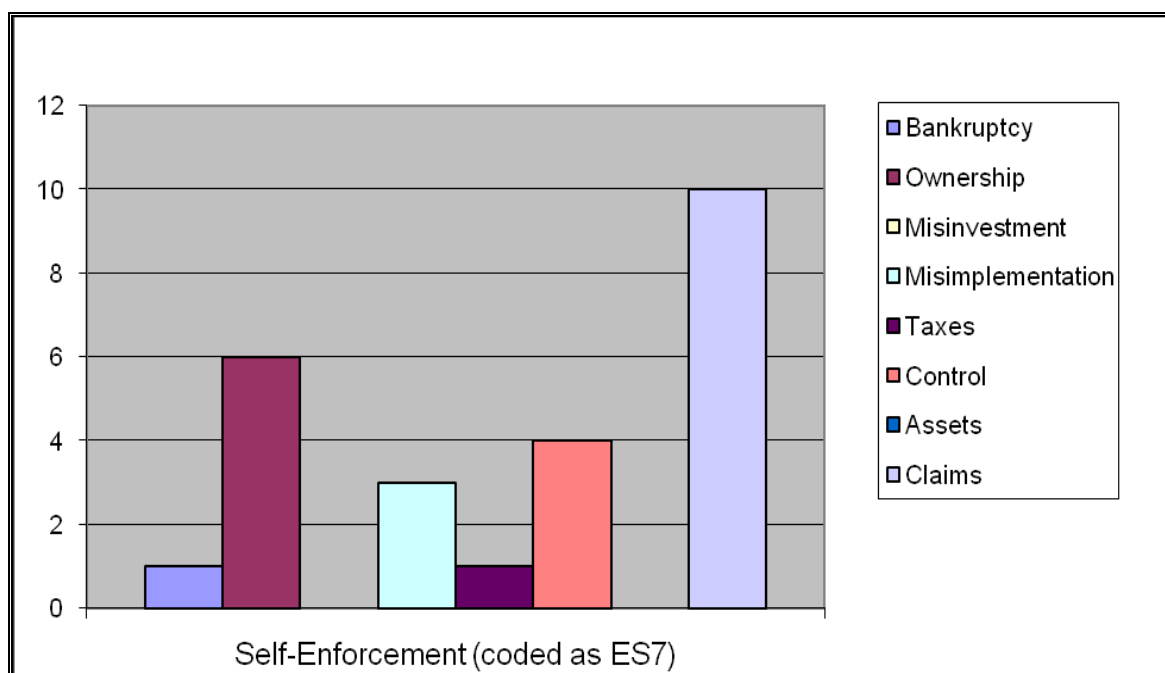


Table 4.17: *Self-Enforcement, 1998*

Companies	No of Articles	Reference Appendix 9a	Second Order Code
Rosneft	1	<i>ref. 10.3</i>	Control
Gazprom	1	<i>ref. 11.1</i>	Ownership
Yukos	1	<i>ref. 12.2</i>	Diversion of Claims
Yukos	2	<i>ref. 12.7</i>	Taxes
<b>Transneft</b>	<b>7</b>	<i>ref. 18</i>	Diversion of Claims
<b>Sidanko</b>	<b>6</b>	<i>ref. 22.1</i>	Diversion of Claims
<b>Krasnoyarsk Hydro Plant</b>	<b>4</b>	<i>ref. 24</i>	Diversion of Claims, Control
Mosenergo	1	<i>ref. 26</i>	Diversion of Claims
Norilsk Nickel	1	<i>ref. 28.2</i>	Diversion of Claims, Control
Novolipetsk	3	<i>ref. 29.2</i>	Diversion of Claims, Control
Magnitogorsk	3	<i>ref. 33</i>	Ownership

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Knauf	1	<i>ref. 36.1</i>	Control, Ownership
Vyborg Paper	3	<i>ref. 39</i>	Ownership, Misimplementation
MOST Bank	1	<i>ref. 43</i>	Misimplementation, Diversion of Claims
Pioneer Group	1	<i>ref. 44</i>	Diversion of Claims
EBRD	1	<i>ref. 45</i>	Bankruptcy
Lomonosov Porcelain Factory	1	<i>ref. 53</i>	Ownership
Kuznetsky Mine	1	<i>ref. 54</i>	Ownership, Misimplementation
Post Office	1	<i>ref. 57</i>	Diversion of Claims

In the majority of cases self-enforcement amounted to blocked resolutions (Yukos, Sidanko, Novolipetsk), heated debates at general meetings and in board rooms (Rosneft, Krasnoyarsk Hydro, Mosenergo) as well as exit in apparent defeat (Norilsk Nickel, Novolipetsk, MOST Bank, Pioneer Bank, EBRD). However, there were a number of extreme measures that parties to the conflict opted to take. The first example is when thousands of irate workers and citizens in the Siberian town of Neftegansk blocked Yukos' President Sergei Muravlenko and other company officials inside a meeting room for 12 hours, demanding settlement of local taxes and wages. A similar case took place at Vyborg Paper Mill when the unions encouraged seizure of the factory's building and blockage of a vital motorway to prevent new owners from making compulsory redundancies. Additionally, managers at Transneft forced employees to sell their shares at a discount or face unpleasant consequences<sup>108</sup>. Last, but not least, is the example of how Knauf, the rightful owner of the Kubansky Gyps-Knauf gypsum mine, refused to leave the office as a renegade director attempted to seize control over the company. The Germans barricaded themselves in the building believing that physical possession

<sup>108</sup> Management used the tactics of intimidation such as threats of being fired, refusal to issue ownership certificates, and deprivation of social benefits if the workers refused to sell.

was more valuable than meaningless court orders. Eventually, the tactics proved effective and the Germans regained control over the factory.

In 2006 there were considerably fewer examples of self-enforcement reported in the newspaper. Coupled with a decline in relationship-based resolution, this serves as an indication of the fact that in 2006 companies relied more on external means of enforcement. This aspect will be considered shortly.

Graph 4.29: *Self-Enforcement, 2006*

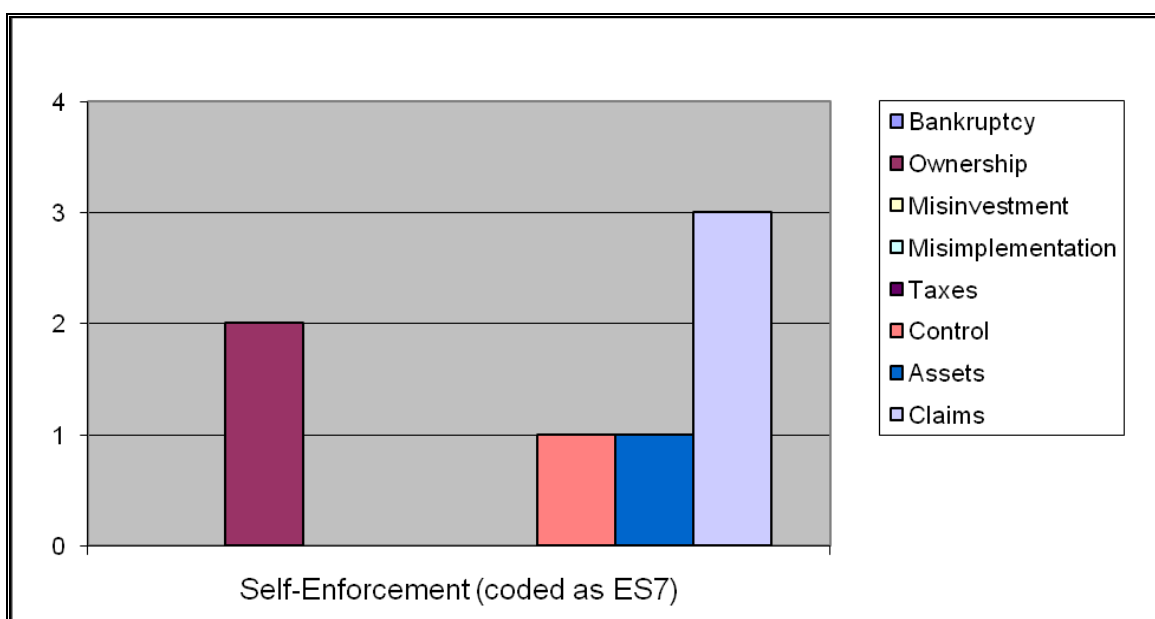


Table 4.18: *Self-Enforcement, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
Yukos	1	<i>ref. 12.5</i>	Diversion of Assets
Yukos	2	<i>ref. 12.7</i>	Control
LUKoil	2	<i>ref. 17.2</i>	Diversion of Claims
Novolipetsk	1	<i>ref. 29</i>	Diversion of Claims, Ownership
Severstal	2	<i>ref. 30.1</i>	Diversion of Claims, Ownership

In 2006 all of the examples of self-enforcement were positive except Yukos' when the company was effectively split into overseas and Russian units. There were endless general meetings and board room battles with foreign investors fighting a doomed battle with the Russian government. In one instance, a foreign unit's board of directors sacked its member for allegedly overseeing a transfer pricing scheme only to see his promotion on the Russian side of the fence. However, cases involving LUKoil, Novolipetsk and Severstal demonstrate that when it comes to private companies, minority shareholders and creditors can in fact exert adequate pressure on the management in order to protect their interests.

According to the above analysis the two years of the study differ substantially with reference to the category of self-enforcement. This difference manifests itself not only through fewer reported examples of the category, but also in the fact that 2006 saw a much more developed resolution process. There were no instances of 'barbarian' behaviour so vividly portrayed by the Knauf ordeal, nor were there any examples of severe union actions reported in 1998. Therefore, in terms of foreign investor perception, it is possible to conclude that in 2006 the situation improved drastically, particularly in relation to private companies' conduct that showed a more balanced cooperation between the stakeholders in question. The reasons for such an encouraging trend could be related to improvements in the formal institutions which have become more effective at protecting investor rights in the instances of blatant violations. Additionally, the wishes of private owners to improve their corporate image may have produced an incentive to resort to more socially acceptable means of enforcement.

#### **4.1.3 Third-Party Enforcement**

Third-party enforcement refers to actions taken by outside entities (other than courts, governmental agencies and designated institutions) aimed at representing the interests of one of the parties in a corporate dispute. These third parties may be acting in their own self-interest as well or may simply be protecting/promoting a friendly organisation.

In 1998 there were 26<sup>109</sup> examples of a third-party involvement in deciding the fate of a corporate dispute. Further details of the category are presented below.

Graph 4.30: *Third-Party Enforcement, 1998*

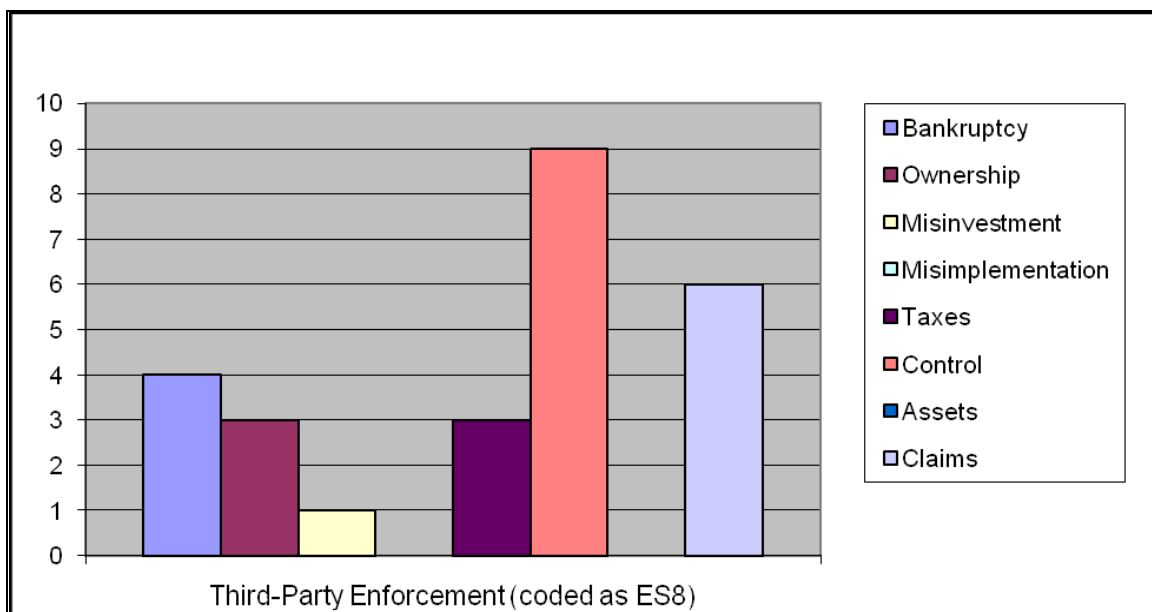


Table 4.19: *Third-Party Enforcement, 1998*

Companies	No of Articles	Reference Appendix 9a	Second Order Code
GAZ	1	ref. 7	Taxes
KIA	1	ref. 9	Taxes, Diversion of Claims
Gazprom	1	ref. 11.3	Ownership
Yukos	1	ref. 12.9	Diversion of Claims
Surgutneftegaz	2	ref. 19	Diversion of Claims
Tatneft	1	ref. 20	Bankruptcy
Sibneft	1	ref. 21.1	Control
Sidanko	2	ref. 22.5	Control, Bankruptcy

<sup>109</sup> 19 separate disputes, 7 of which were parallel coded.

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
<b>Tyumen</b>	<b>7</b>	<i>ref. 23</i>	Control
<b>Krasnoyarsk Hydro Plant</b>	<b>4</b>	<i>ref. 24</i>	Diversion of Claims, Control
Electrosila	1	<i>ref. 27</i>	Control
Novolipetsk	3	<i>ref. 29.2</i>	Diversion of Claims, Control
Magnitogorsk	3	<i>ref. 33</i>	Ownership
Achinsk Alumina Combine	1	<i>ref. 35</i>	Bankruptcy, Misinvestment, Control
Knauf	1	<i>ref. 36.2</i>	Taxes, Control
<b>AssiDoman</b>	<b>6</b>	<i>ref. 38.2</i>	Ownership
Inkombank	1	<i>ref. 42</i>	Control
Channel 5	1	<i>ref. 50</i>	Diversion of Claims
ORT	1	<i>ref. 51.2</i>	Bankruptcy

In 1998 there were a number of outside forces to be reckoned with in the corporate arena. The first, and probably most visible force, were the Financial Industrial Groups who on the one hand protected and watched over their friendly organisations (Yukos' Menatep, and Achinsk Alumina Combine' KRAZ as well as financial structures behind Novolipetsk) and on the other were instrumental in redistributing claims, often to their own advantage (Sibneft, Sidanko, Tyumen, Krasnoyarsk Hydro, Electrosila and AssiDoman). From the reported material in 1998 it was evident that the Financial Industrial Groups (FIG) were capable of negotiating the environment much more effectively than smaller entities and foreign investors. In a dispute over the replacement of a director of Electrosila, EMK (the FIG that instigated the action) simply ignored the decision of a court that had ruled that the replacement of the director was unlawful. Siemens, the other party to the conflict, was predicted by analysts to lose in the conflict purely because of the power of EMK. Moreover, in a dispute over the Kranoyarsk Hydro Plant, Tanako (a local FIG) took on the government in a fight for control of a 23%

stake in the plant. In 1998 the only match for enforcement powers of a FIG was another FIG. In a conflict over Inkombank's assets when two banking empires clashed, court rulings were the deciding factor because of the equal clout of the affected power structures.

In addition, foreign creditors were very powerful in the 1990s. It was the IMF and the World Bank that demanded tax and industry reforms in the country before releasing their financial support. These organisations were influential arbitrators in particularly large corporate conflicts with national interests at stake. Moreover, on a slightly smaller scale, a lot of foreign creditors managed to negotiate substantial stakes in major Russian corporations as collateral for the loans that were often never going to be repaid. Although Russian organisations frequently illegally expropriated such collateral (Yukos), or even failed to transfer it (Magnitogorsk), foreign creditors were nevertheless a force to consider in certain corporate disputes at the time (Tatneft).

Finally, unidentified (possibly criminal) groups were also important power structures at the time. These groups acted in concert with tax authorities (KIA Motors, Knaufl), courts (AssiDoman) and local administration (Surgutneftegaz). Due to their suspected illegal nature, very little was known about the way these entities functioned in the environment. Nevertheless, their influence was constantly discussed in the reported material.

Conversely, in 2006 only three examples of third-party enforcement were extracted from the Moscow Times reports. This is the smallest dispute resolution category.

Graph 4.31: *Third-Party Enforcement, 2006*

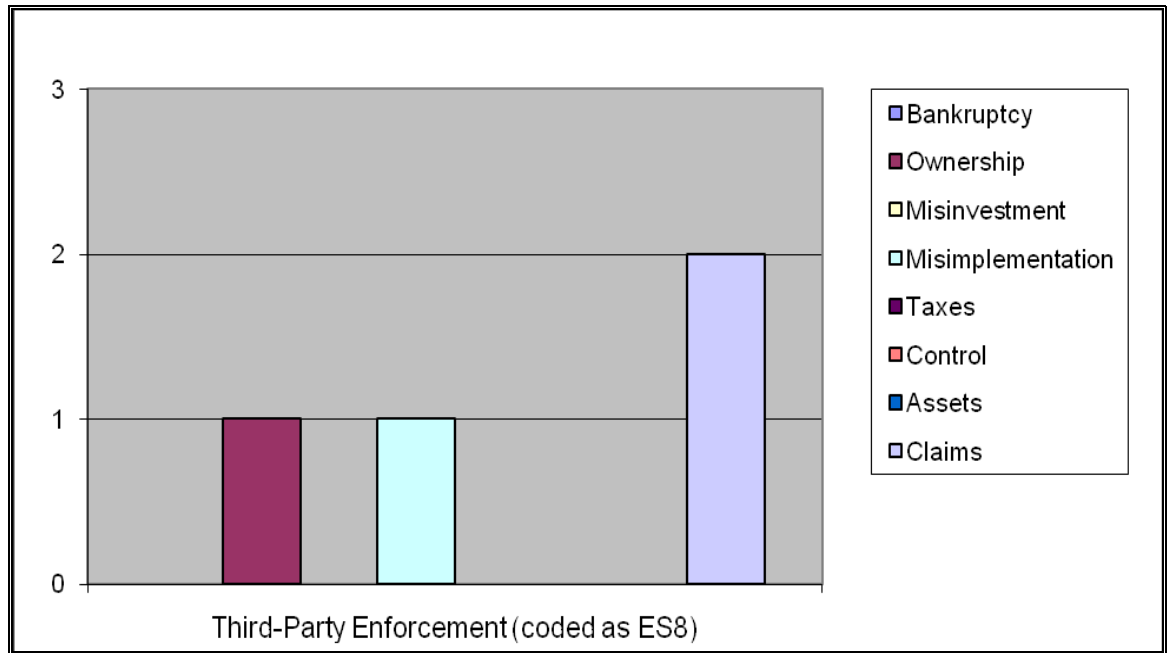


Table 4.20: *Third-Party Enforcement, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
RusAl	3	ref. 32.3	Control
Eurocement	1	ref. 37	Diversion of Claims
<b>IKEA</b>	<b>4</b>	ref. 48	Diversion of Claims, Misimplementation

However, despite the small number of reported cases falling into this category, all of the sub-themes extracted from the 1998 data were also identified in 2006.

First, Financial Industrial Groups continue to be a powerful arbitrator in the environment. With reference to the conflict involving Eurocement, an American Fund called Russian Partners was forced to recruit the services of A1 (a unit of very powerful Financial Industrial Group Alfa) in order to increase its chances in the battle against a large scale expropriation. A single reported example of this kind of a corporate dispute resolution probably signifies that there was a greater degree of clarity in terms of who arbitrates and helps to resolve corporate conflicts in 2006. Moreover, from the reported material it was apparent that the FIGs like



Alfa Group started offering formal services to smaller corporate entities that are aimed at increasing chances of a fairer resolution on the most basic level of an association with a powerful structure.

In terms of the role of foreign creditors, RusAl's example of ownership disclosure reveals a positive outcome of engaging with outside finance providers. The European Bank for Reconstruction and Development and the International Financial Corporation forcefully persuaded the company to disclose its ownership structure using the \$150m. loan as a bargaining tool. Although Russian companies were less desperate for outside finance in 2006 (a proposition based on the reduced number of associated disputes) there were understandable incentives for them in maintaining constructive partnerships with foreign investors (as demonstrated by the RusAl's example). The size of this incentive is directly proportionate to the enforcement powers that international creditors (and shareholders) can justifiably rely on in the Russian context.

Finally, and perhaps not so encouragingly, anonymous power structures continue to be active in the environment. The example of IKEA was no different to the 1998 disputes involving KIA, AssiDoman and Surgutneftegaz. Corporate raids involving a collusion among a usually unidentified 'business group' and authorities (in the case of IKEA it was fire inspectorate) remained a strong feature of the perceived environment<sup>110</sup>.

### 3.1.4 Private Enforcement

Private enforcement<sup>111</sup> is the crudest form of corporate dispute resolution when affected parties resort to extra judiciary behaviour. Normally, such undue pressure

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<sup>110</sup> Raiders, as they are often referred to, bribe various inspectorates who conduct checks of target companies. Taking advantage of vaguely worded regulations (fire code, health and safety, employment law, environmental law) inspectors always achieve the task of finding 'severe violations'. When the inspectors threaten the closure of the business, a buyer (raiders) suddenly appears offering a highly discounted price for the assets. These tactics are used to take over business, force sales of key assets, put pressure on competitors as well as for political reasons.

<sup>111</sup> Private security firms have evolved from criminal groups (typical in 1990s) to licensed organisations that offer a range of security services. However, in terms of the conduct of these organisations, little change occurred. Often, fully licensed security firms employ bandit practice and engage in extra judiciary forms of enforcement.

is exerted on behalf of the stakeholders involved and often leads to violence or physical threats.

In 1998 there were 12 examples<sup>112</sup> of such behaviour reported in the Moscow Times. Similar to most of the categories, ownership and control disputes represent the most pronounced connection with the second order codes.

Graph 4.32: *Private Enforcement, 1998*

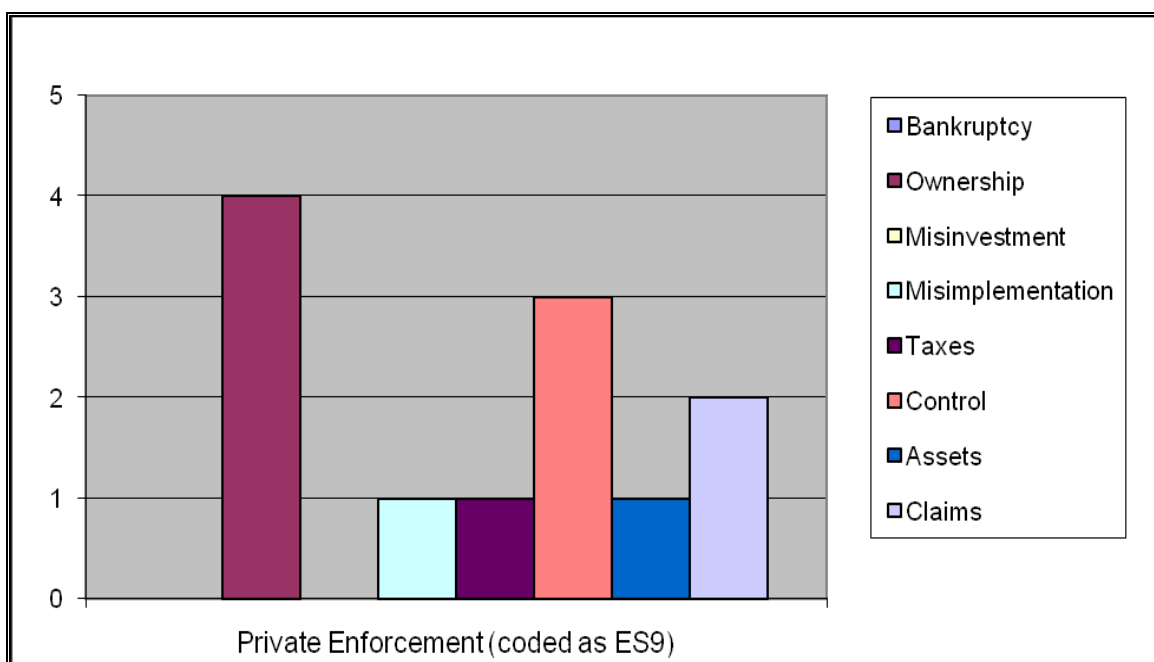


Table 4.21: *Private Enforcement, 1998*

Companies	No of Articles	Reference Appendix 9a	Second Order Code
VimpelCom	2	ref. 4	Control
AvtoVaz	1	ref. 6	Diversion of Claims
Yukos	2	ref. 12.7	Taxes
Surgutneftegaz	2	ref. 19	Diversion of Claims
Knauf	1	ref. 36.1	Control, Ownership
<b>Subway</b>	<b>7</b>	ref. 52	Control, Diversion of Assets, Control

<sup>112</sup> 8 separate disputes of which 4 were parallel coded.

Lomonosov Porcelain Factory	1	<i>ref. 53</i>	Ownership
Kuznetsky Mine	1	<i>ref. 54</i>	Ownership, Misimplementation

In terms of the content, in 1998 examples of private enforcement revealed the most extreme behaviour by affected parties. When AvtoVAZ CEO Mr. Kadannikov announced a campaign to renegotiate suspect sales margins by the dealers, the company's deputy commercial director was murdered and the director of the spare parts centre was severely beaten. In another reported example, a popular mayor of a town of residence for one of Yukos's subsidiaries was killed after he criticised the company for many of the town's problems. Additionally, VimpelCom's employees received death threats and were physically assaulted at the time when influential stakeholders were fighting for control over the company that was benefiting from booming growth. Similar events occurred at Lomonosov Porcelain Factory and Kuznetsky Mine when employees were beaten up and corporate property was destroyed amid a fight for control and ownership. In the instance of the latter, local administration and federal agencies were alleged by the newspaper to be the perpetrators of these actions. Finally, slightly more subtle, but by no means less forceful use of this enforcement strategy was demonstrated by the role of a private bodyguard at the Subway – Minutka conflict, the use of the Cossack army in the Knauf dispute and finally, the blackmailing practice of a police department with reference to Standart NMT. This practice is very difficult to resist without resorting to similar measures of extra-judiciary enforcement.

In 2006 there were 9 examples of private enforcement. However, these were reported with reference to only 4 separate disputes with the remaining 5 representing parallel coding in the hierarchy.

Graph 4.33: *Private Enforcement, 2006*

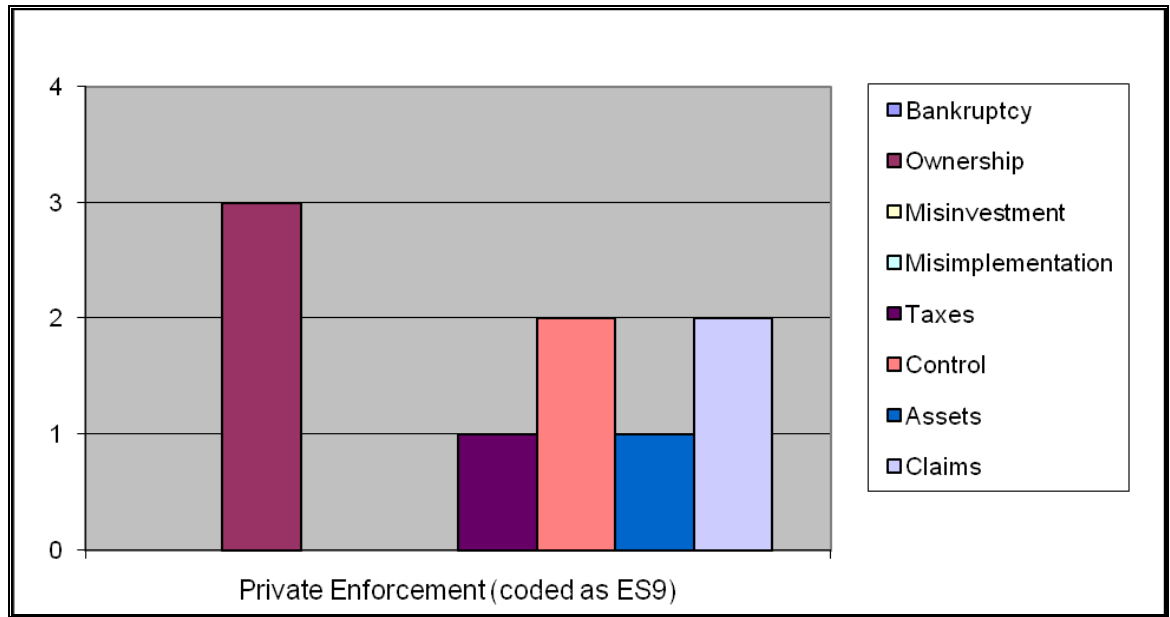


Table 4.22: *Private Enforcement, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
<b>Gazpom</b>	<b>4</b>	<i>ref. 11.5</i>	Diversion of Claims, Ownership
<b>Yukos</b>	<b>23</b>	<i>ref. 12.1</i>	Ownership, Control, Taxes
Yukos	2	<i>ref. 12.2</i>	Diversion of Claims
<b>TNK-BP</b>	<b>15</b>	<i>ref. 16.1</i>	Control, Ownership, Diversion of Assets

In terms of the content, this category was completely dominated by the way the Russian government dealt with the re-nationalisation of Yukos. On the one hand, there were a number of extradition cases filed by the Russian government against former Yukos employees accusing them of attempted murder (Nevzlin) and large scale fraud (Golubovich). However, on the other hand, there were reports suggesting that the Russian government initiated a campaign of intimidation against Yukos employees and their lawyers. According to numerous reports jailing and beatings were used in order to force confessions and silence Russian lawyers

and extradition procedures against foreign employees and lawyers. As far as investor perception is concerned however, the Russian government was reported as being the main violator in this conflict<sup>113</sup> with American courts trying to serve top Russian officials with the help of an Irish private investigation firm. Additionally, there were instances of a criminal involvement in RosUkrEnergo dealings and a suspected contract killing of a TNK-BP official.

Collected data suggests that although there were fewer reported instances of this category in 2006, the extent of perceived violence with regard to corporate affairs in the country did not change. However, it has to be acknowledged that the origin of this form of enforcement evolved substantially. In 1998 there were a number of isolated examples of this category with reference to private entities whereas in 2006 private enforcement, as described above, radiated from the government itself. The latter proposition is re-enforced by the substantial amount of coverage associated with Yukos and TNK-BP examples.

#### **4.1.5 Administrative Levers of the State**

According to the reported content this category refers to situations when the government acts as an arbitrator of corporate disputes. This category is different to state interference in that here, the state is not necessarily party to a dispute and the emphasis is more on the actual actions that officials take. This category identifies tools (administrative levers) that officials resort to with reference to the process of dispute resolution in the respective environments. An example of the use of administrative levers would be an official assisting a friendly business with applying for a licence or state funding in its minor form and active interference in the formal process of dispute resolution in its most crude format.

In 1998 a large proportion of corporate disputes were resolved by the government on both local and federal levels. Although this process was not always to the mutual interest of the parties involved it nevertheless complemented the judiciary and at times was the only workable approach to a dispute resolution. As depicted

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<sup>113</sup> Possibly, this is where the pro foreign bias of the newspaper played a significant role in the way this particular dispute was covered.

in graph 4.34, the Russian government used its influence primarily with reference to control, diversion of claims and ownership disputes.

Graph 4.34: *Administrative Levers of the State, 1998*

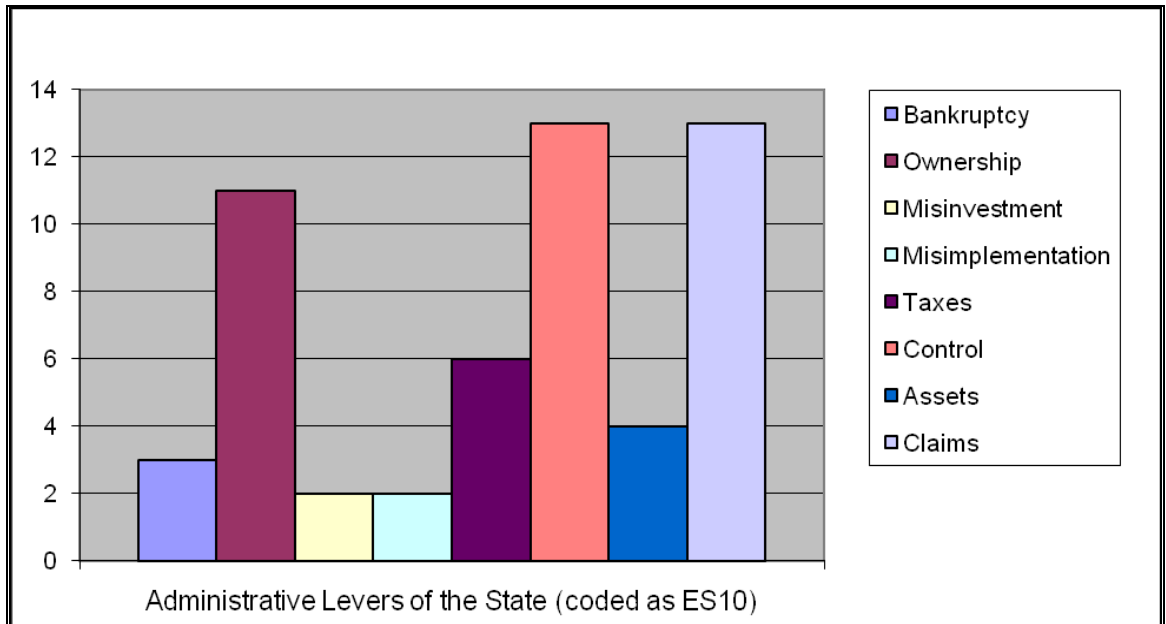


Table 4.23: *Administrative Levers of the State, 1998*

Companies	No of Articles	Reference Appendix 9a	Second Order Code
Aeroflot	1	<i>ref. 1</i>	Diversion of Claims
<b>MGTS</b>	<b>4</b>	<i>ref. 3</i>	Diversion of Claims
VimpelCom	2	<i>ref. 4</i>	Control
KIA	1	<i>ref. 9</i>	Taxes, Diversion of Claims
<b>Rosneft</b>	<b>8</b>	<i>ref. 10.1</i>	Diversion of Assets
Gazprom	3	<i>ref. 11.2</i>	Taxes
Gazprom	1	<i>ref. 11.6</i>	Diversion of Assets
Yukos	2	<i>ref. 12.5</i>	Ownership
Yukos	2	<i>ref. 12.6</i>	Misimplementation

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Yukos	2	<i>ref. 12.7</i>	Taxes
<b>Transneft</b>	<b>7</b>	<i>ref. 18</i>	Diversion of Claims
Surgutneftegaz	2	<i>ref. 19</i>	Diversion of Claims
Sibneft	1	<i>ref. 21.1</i>	Control
Sibneft	1	<i>ref. 21.3</i>	Ownership
<b>Sidanko</b>	<b>6</b>	<i>ref. 22.1</i>	Diversion of Claims
<b>Sidanko</b>	<b>4</b>	<i>ref. 22.2</i>	Taxes
Sidanko	2	<i>ref. 22.3</i>	Control, Taxes
<b>Tyumen</b>	<b>7</b>	<i>ref. 23</i>	Control
<b>Krasnoyarsk Hydro</b>	<b>4</b>	<i>ref. 24</i>	Diversion of Claims, Control
<b>UES</b>	<b>11</b>	<i>ref. 25.1</i>	Control
<b>UES</b>	<b>4</b>	<i>ref. 25.2</i>	Control
<b>UES</b>	<b>8</b>	<i>ref. 25.4</i>	Ownership
Norilsk Nickel	<b>1</b>	<i>ref. 28.1</i>	Ownership
Novolipetsk	3	<i>ref. 29.2</i>	Diversion of Claims, Control
Magnitogorsk	3	<i>ref. 33</i>	Ownership
Lebedinsky Ore Mining Plant	2	<i>ref. 34.1</i>	Ownership
Lebedinsky Ore Mining Plant	1	<i>ref. 34.2</i>	Diversion of Claims
Achinsk Alumina Combine	1	<i>ref. 35</i>	Bankruptcy, Misinvestment, Control
Knauf	1	<i>ref. 36.1</i>	Control, Ownership
AssiDoman	2	<i>ref. 38.1</i>	Taxes
<b>AssiDoman</b>	<b>6</b>	<i>ref. 38.2</i>	Ownership

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Vyborg Paper	3	<i>ref. 39</i>	Ownership, Misimplementation
<b>SBS Agro</b>	<b>4</b>	<i>ref. 40.1</i>	Diversion of Claims
<b>SBS Agro</b>	<b>5</b>	<i>ref. 40.2</i>	Bankruptcy
SBS Agro	1	<i>ref. 40.3</i>	Misinvestment
MFK Renaissance	1	<i>ref. 41</i>	Control
Channel Five	1	<i>ref. 50</i>	Diversion of Claims
ORT	1	<i>ref. 51.1</i>	Diversion of Claims
ORT	1	<i>ref. 51.2</i>	Bankruptcy
<b>Subway</b>	<b>7</b>	<i>ref. 52</i>	Control, Diversion of Assets, Ownership
MCCI	1	<i>ref. 55</i>	Control, Diversion of Assets, Ownership
Standart NMT	1	<i>ref. 56</i>	Diversion of Claims

In terms of the content of this category, an important distinction between local and federal government's involvement needs to be drawn. According to the reported material, 9 disputes were influenced by local governments (KIA, Yukos, Surgutneftegaz, Sibneft, Sidanko, Lebedinsky Ore Mining Plant, Achinsk Alumina Combine, Knauf, Subway and Standart NMT). In general such an influence manifested itself through legal assistance, i.e. local administration had a significant capacity to ensure that local courts return rulings favourable for a certain party. In a dispute over a St. Petersburg subsidiary of Surgutneftegaz, it was reported that the parent could not achieve anything through the local courts, simply because the administration was not on its side. In a conflict involving Achinsk, the local courts readjusted their vision of the situation consistently with the changing opinion of the governor. A similar point was made with reference to reported conflicts involving Sibneft, Lebedinsky Ore Mining Plant and Knauf. Moreover as demonstrated by the Subway dispute, the local government could influence the process of resolution by complete disengagement even after the wrongdoer had been



determined by both international and local courts. In this sense, parties to the conflict could rely on technicalities such as an emergency change of nominal ownership in order to cancel out rulings on the substance of the matter. The key point here is that local administrations often tolerated small scale corruption that made it possible for example to re-register businesses in a matter of hours. Selective reprimanding (or non-reprimanding) of such behaviour within the system represented a very effective administrative resource that ensured pre-determined resolutions. The Russian partners in the Subway dispute changed the name of the registered entity, and on those grounds refused to follow orders of the court. The local administration did not intervene. Moreover, disputes involving KIA and Standart NMT demonstrate how tax authorities and police departments followed the same pattern of behaviour.

On the federal level, there were examples of a similar nature where allegations against certain people were dropped (Aeroflot, UES) and laws were applied selectively, MGTS, VimpelCom. Similar to the nature of engagement of local administrations, the key to administrative levers was in the right associations with government officials. A conflict involving AssiDoman was a very good practical demonstration of the latter point when the company felt it was necessary to cease production in the wake of the government reshuffle. According to the Moscow Times reports this was a precautionary measure determined by the loss of the aforementioned association. Furthermore, if such association was missing or destroyed, companies were in danger of being forced out of business by means of 'manufactured' allegations in the same manner as Trans World lost its ground in the conflict with the new owners of Novolipetsk. In this particular example, the 'manufactured' allegations were against the Trans World director who was accused of spying. The company's problems coincided with the sacking of a government official who was connected to Trans World. Lastly, the government resorted to the use of administrative levers in order to punish non-conformist behaviour of power structures which was rather typical in 1998. 'Find and punish' instructions by the president were frequently heard (Rosneft, UES, Magnitogorsk, Lebedinsky Ore Mining Plant), but sometimes amounted to populist exclamations with severely delayed or limited impact (Knauf, Magnitogorsk). The latter point

exposed a gap in the federal government's grip over corporate affairs in the country in 1998.

In 2006 the intensity of reported material falling into this category remained high. The government continued to use administrative levers while influencing the resolution of reported corporate conflicts falling into a wide range of second order codes.

Graph 4.35: *Administrative Levers of the State, 2006*

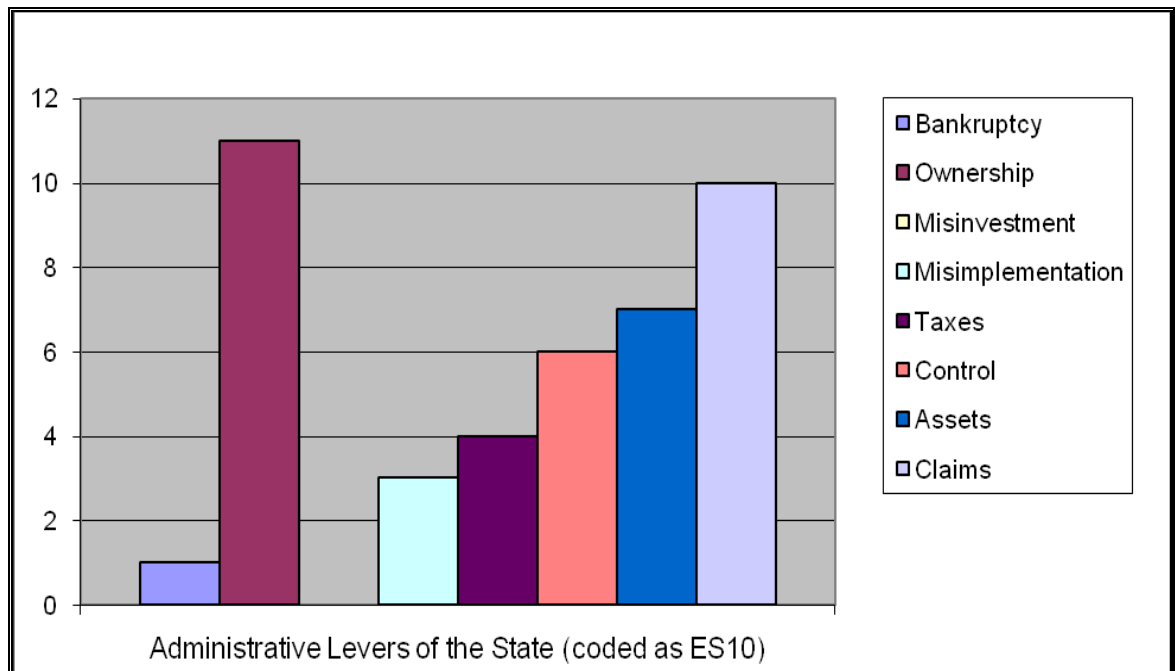


Table 4.24: *Administrative Levers of the State, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
Aeroflot	1	ref. 1	Diversion of Claims
Svyazinvest	1	ref. 2	Ownership
MegaFon	2	ref. 5	Diversion of Claims, Ownership
AvtoVaz	2	ref. 6	Control, Taxes
Rosneft	2	ref. 10.1	Diversion of Claims
<b>Rosneft</b>	<b>11</b>	ref. 10.3	Diversion of Claims, Diversion of Assets

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9b</b>	<b>Second Order Code</b>
Rosneft	1	<i>ref. 10.4</i>	Taxes
<b>Rosneft</b>	<b>6</b>	<i>ref. 10.5</i>	Diversion of Claims, Diversion of Assets
Gazprom	1	<i>ref. 11.1</i>	Ownership
Gazprom	1	<i>ref. 11.2</i>	Diversion of Assets, Diversion of Claims
<b>Gazprom</b>	<b>4</b>	<i>ref. 11.3</i>	Diversion of Assets, Ownership
Gazprom	1	<i>ref. 11.4</i>	Control
<b>Gazprom</b>	<b>4</b>	<i>ref. 11.5</i>	Diversion of Claims, Ownership
<b>Yukos</b>	<b>23</b>	<i>ref. 12.1</i>	Ownership, Control, Taxes
Yukos	1	<i>ref. 12.3</i>	Diversion of Claims
<b>Yukos</b>	<b>8</b>	<i>ref. 12</i>	Bankruptcy
<b>Yukos</b>	<b>6</b>	<i>ref. 12.6</i>	Diversion of Assets
Yukos	2	<i>ref. 12.7</i>	Control
<b>Shell</b>	<b>25</b>	<i>ref. 13</i>	Misimplementation, Ownership, Diversion of Assets
Total	2	<i>ref. 14</i>	Ownership, Diversion of Claims
ExxonMobil	2	<i>ref. 15</i>	Control
<b>TNK-BP</b>	<b>15</b>	<i>ref. 16.1</i>	Control, Ownership, Diversion of Assets
TNK-BP	1	<i>ref. 16.2</i>	Taxes
LUKoil	2	<i>ref. 17.1</i>	Ownership
<b>Severstal</b>	<b>4</b>	<i>ref. 30.2</i>	Misimplementation
RusAl	1	<i>ref. 32.4</i>	Ownership
<b>IKEA</b>	<b>4</b>	<i>ref. 48</i>	Diversion of Claims, Misimplementation

According to the reported material, administrative levers of the state were used in much the same way in 2006. The only noticeable change was in the emergence of the monopoly of the federal government which did not allow local administrations to take any advantage of enforcement powers without the warrant of the former. On one occasion, the Nenez governor was detained on suspicion of fraud and embezzlement allegedly after/because he complained against a Rosneft's subsidiary (state owned) which did not pay taxes and broke ecological standards. Conversely, the federal government demonstrated an ever growing capacity to influence the judiciary with an unprecedented intensity. Additionally, the government relied on the services of various state agencies while orchestrating a mass re-allocation of ownership within the strategic sector. The state agencies that were frequently referred to by the newspaper were the tax authorities (Yukos), the National Resources Ministry (Shell, TNK-BP, LUKoil), the Sub-soil Resources Agency (Total), the Federal Service for Ecological, Technological and Atomic Inspection (ExxonMobil), the Prosecutor General's Office (TNK-BP). These disputes received a great deal of coverage making a substantial impact on the way the environment was perceived in 2006.

The biggest difference between the two years of the study is the ever growing amount of the state's command of its own ministries and institutions. In 1998 these did not function in unison with, for example, tax authorities attempting to bankrupt state entities and local administrations hunting for anything valuable in its vicinity. This was not the case in 2006 when there were a number of examples indicating that such instances of insubordination stopped happening. Nevertheless there were examples of a suspected corrupt use of public institutions (IKEA's troubles over fire code violations) apparently unconnected to the federal government. However, such behaviour was not in the way of the re-nationalisation agenda, and could have been interpreted as an imitation of the above described approach but on a smaller scale.<sup>114</sup>

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<sup>114</sup> IKEA's trouble over fire violations was a classic example of a corporate raid when the fire inspectorate acted on behalf of a third party (see appendix 9b, template 48).

#### 4.1.6 Shadow of Enforcement

This category refers to examples where the threat of referring to a potential arbitrator is in itself a way of resolving a corporate dispute. Typically, this relates to situations where a disadvantaged party makes it known to a benefiting party that if the situation is not corrected, a certain action (suit, private enforcement, or third-party involvement) will be taken.

In 1998 there were 8 examples<sup>115</sup> of this type of enforcement extracted from the Moscow Times. Diversion of claims is the most significant second order code with misimplementation, taxes and control also represented with one instance each (graph 4.36 and table 4.25).

Graph 4.36: *Shadow of Enforcement, 1998*

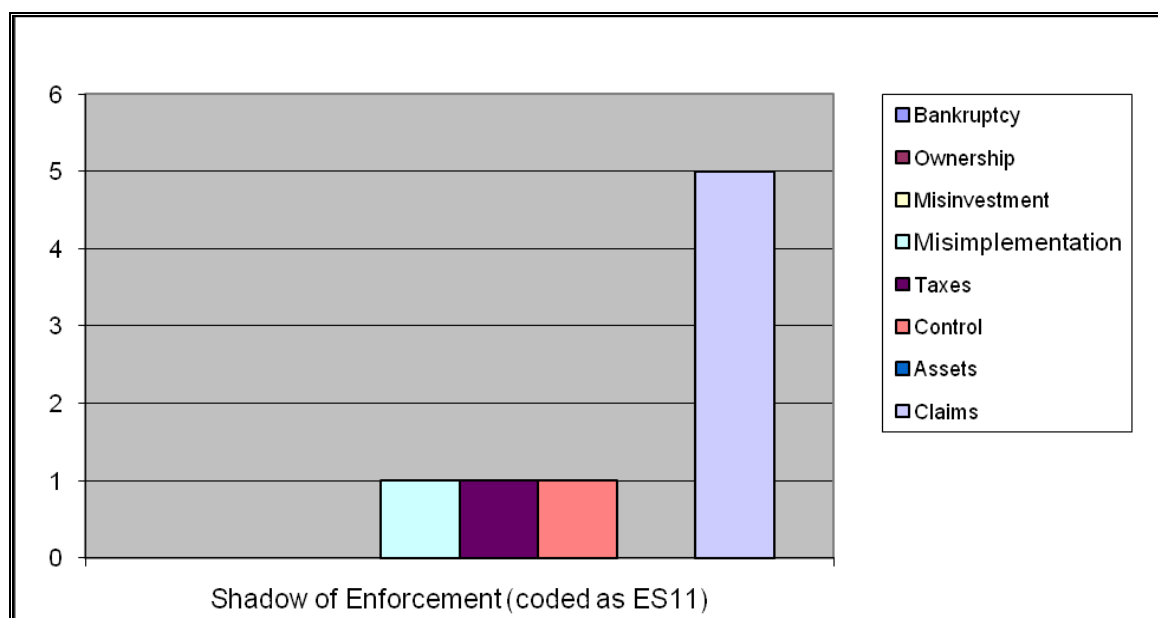


Table 4.25: *Shadow of Enforcement, 1998*

Companies	No of Articles	Reference Appendix 9a	Second Order Code
Aeroflot	1	ref. 1	Diversion of Claims
Gazprom	3	ref. 11.2	Taxes

<sup>115</sup> 7 separate disputes of which one was parallel coded.

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Yukos	1	<i>ref. 12.3</i>	Diversion of Claims
Yukos	1	<i>ref. 12.4</i>	Diversion of Claims
<b>UES</b>	<b>11</b>	<i>ref. 25.1</i>	Control
UES	1	<i>ref. 25.3</i>	Diversion of Claims
MOST Bank	1	<i>ref. 43</i>	Misimplementation, Diversion of Claims

In relation to the content of the reported material, minority shareholders and other stakeholders threatened legal action a number of times (Yukos, Most Bank and Aeroflot). It was very difficult to determine the effectiveness of such a move, but the message was frequently very clear. In the instance of the conflict over UES dividends, a shareholder (the National Reserve Bank) said that they would wait and see whether the new management would agree to pay the money. The shareholder also made it clear that if the liability was not settled, the case would be referred to the Russian courts. Additionally, there was a noticeable element of reliance on self-enforcement powers with reference to this category. In other words, stakeholders threatened to instigate punitive actions that they themselves were capable of seeing through. To illustrate the point, the EBRD used the sell option as leverage in persuading the management of Yukos to come up with a credible restructuring plan.

Furthermore, Gazprom proposed that an action taken against the companies' two subsidiaries would lead to far-reaching economic consequences and that the company could exacerbate the negative impact. And finally, threats to reveal the 'truth' about contenders for the top positions at UES very much determined the candidates' actions and behaviour<sup>116</sup>.

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<sup>116</sup> Threats came from the candidates themselves and their respective political clans.

In the more recent year of the study, there were also 8 examples<sup>117</sup> of shadow of enforcement with a wider spread of matching second order codes largely due to a greater degree of parallel coding. Graph 4.37 and table 4.26 provide further details of the reported material.

Graph 4.37: *Shadow of Enforcement, 2006*

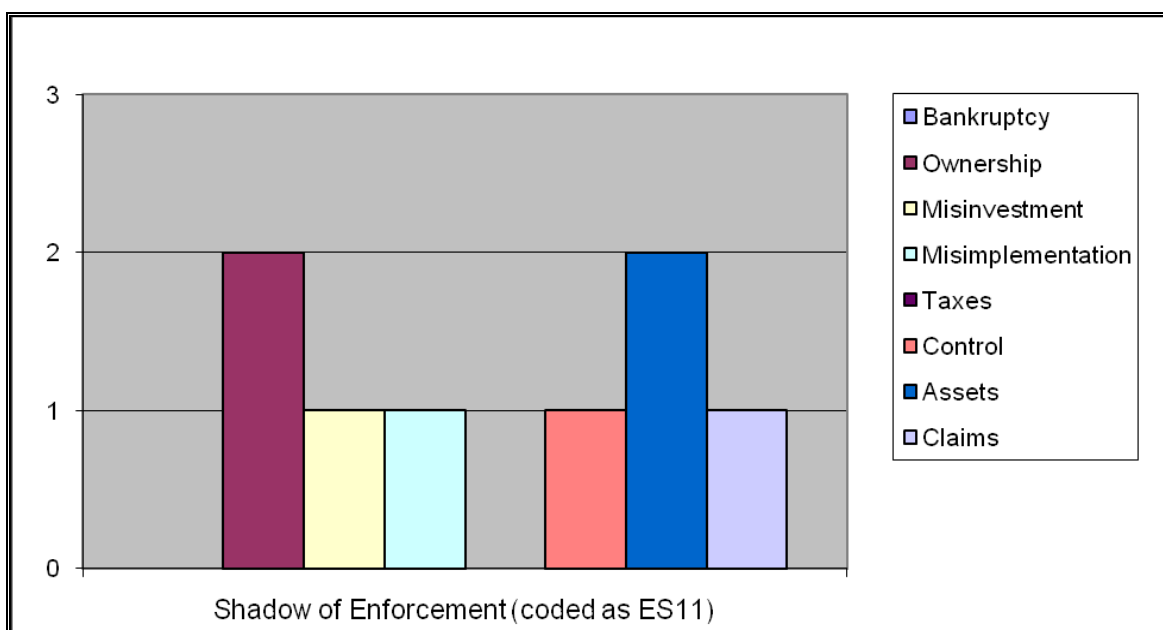


Table 4.26: *Shadow of Enforcement, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
VimpelCom	1	ref. 4	Misinvestment
Rosneft	3	ref. 10.2	Diversion of Claims
<b>Shell</b>	<b>25</b>	ref. 13	Misimplementation, Ownership, Diversion of Assets
<b>TNK-BP</b>	<b>15</b>	ref. 16.1	Control, Ownership, Diversion of Assets

<sup>117</sup> 5 separate disputes 3 of which were parallel coded.

In 2006 there were two reported instances when minority shareholders threatened legal action. In the first instance it was the minority of Rosneft who were hopeful that the company would surrender to their requests ahead of the LSE IPO<sup>118</sup>. The second instance was linked to the conflict at VimpelCom where the company's purchasing strategy was disputed by one of its shareholders (Telenor). The key point here is that the shareholder had already filed two suits in the Russian courts and threatened to take the case to a US court. All the remaining cases of this category related to the government and large state companies threatening international oil companies. In all of the reported instances the manufactured threats of licence withdrawal (based on environmental allegations) subsided or altogether evaporated once the projects in question were opened up to state companies. In retaliation, a number of foreign diplomats responded with warnings that foreign direct investment would fall significantly if the Russian government did not clarify the rules of the game in formal terms.

In comparative terms, threats of self-enforcement were not found in reports pertaining to 2006. This fact confirmed a declining role of self-enforcement as previously discussed. Additionally, this suggests that a greater status was attached to external arbitrators and enforcers in 2006 than in 1998. Also in 2006 the threat of foreign (namely US) litigation was used as a powerful message in conflict resolution. Finally, and in consistence with previously discussed categories, the government and state companies demonstrated their growing enforcement powers by simply threatening allegations as a way of persuading private entities to accept their terms of cooperation. In 1998 such examples were visibly missing from the reported material of the Moscow Times.

#### 4.1.7 Litigation

This category refers to instances when courts or other formal institutions are used in the process of corporate dispute resolution. The content of this category reveals the level of perceived adequacy of the court system in Russia and exposes instances when the arbitration is influenced by other parties to the conflict.

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<sup>118</sup> Initial Public Offering and London Stock Exchange



In 1998, litigation was used with reference to a variety of reported conflicts with control, ownership and diversion of claims being the most prominently represented second order codes. Altogether, there were 58 examples<sup>119</sup> when courts and other formal institutions were featured as a resolution mechanism. Further details of the category are presented in graph 4.38 and table 4.27.

Graph 4.38: *Litigation, 1998*

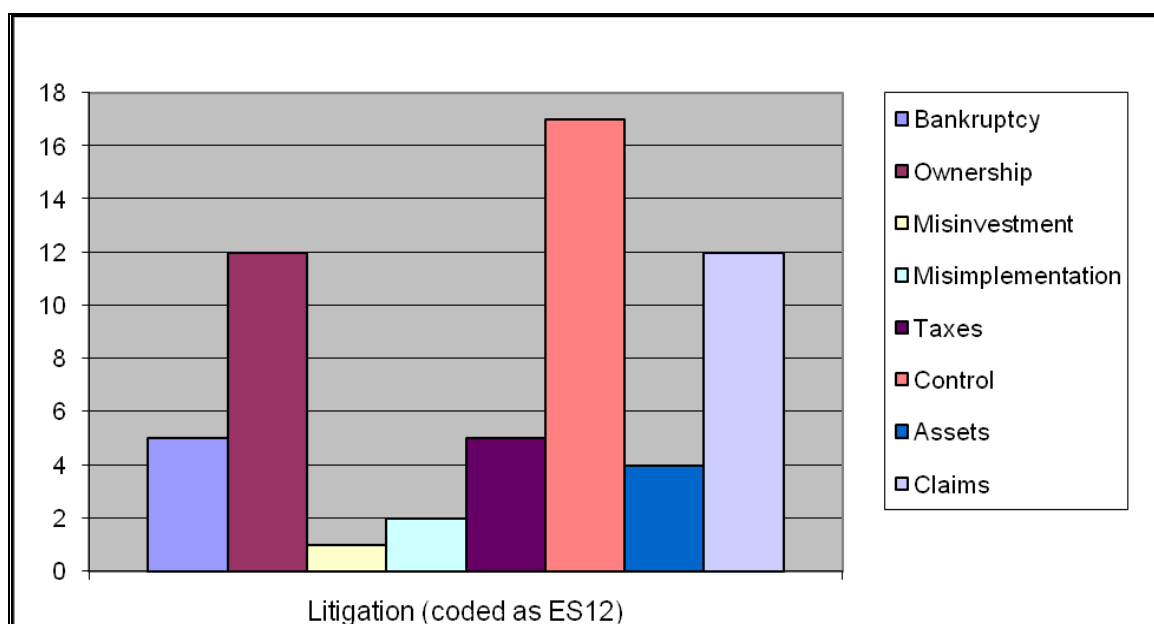


Table 4.27: *Litigation, 1998*

Companies	No of Articles	Reference Appendix 9a	Second Order Code
<b>Rosneft</b>	<b>8</b>	<i>ref. 10.1</i>	Diversion of Assets
Gazprom	1	<i>ref. 11.4</i>	Ownership
<b>Yukos</b>	<b>10</b>	<i>ref. 12.1</i>	Diversion of Claims, Control
Yukos	1	<i>ref. 12.8</i>	Taxes
<b>Transneft</b>	<b>7</b>	<i>ref. 18</i>	Diversion of Claims
Surgutneftegaz	2	<i>ref. 19</i>	Diversion of Claims
Sibneft	1	<i>ref. 21.1</i>	Control, Taxes

<sup>119</sup> 41 separate disputes 16 of which were parallel coded.

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
<b>Sibneft</b>	<b>5</b>	<i>ref. 21.2</i>	Diversion of Claims, Diversion of Assets
<b>Sidanko</b>	<b>6</b>	<i>ref. 22.1</i>	Diversion of Claims
Sidanko	2	<i>ref. 22.3</i>	Control, Taxes
Sidanko	2	<i>ref. 22.4</i>	Bankruptcy
Sidanko	2	<i>ref. 22.5</i>	Control, Bankruptcy
<b>Tyumen</b>	<b>7</b>	<i>ref. 23</i>	Control
<b>Krasnoyarsk Hydro Plant</b>	<b>4</b>	<i>ref. 24</i>	Diversion of Claims, Control
<b>UES</b>	<b>4</b>	<i>ref. 25.2</i>	Control
<b>UES</b>	<b>8</b>	<i>ref. 25.4</i>	Ownership
Electrosila	1	<i>ref. 27</i>	Control
Norilsk Nickel	1	<i>ref. 28.1</i>	Ownership
Norilsk Nickel	1	<i>ref. 28.3</i>	Taxes
<b>Novolipetsk</b>	<b>4</b>	<i>ref. 29.1</i>	Control
Novolipetsk	3	<i>ref. 29.2</i>	Diversion of Claims, Control
Magnitogorsk	3	<i>ref. 33</i>	Ownership
Lebedinsky Ore Mining Plant	2	<i>ref. 34.1</i>	Ownership
Lebedinsky Ore Mining Plant	1	<i>ref. 34.2</i>	Diversion of Claims
Achinsk Alumina Combine	1	<i>ref. 35</i>	Bankruptcy, Misinvestment, Control
Knauf	1	<i>ref. 36.1</i>	Control, Ownership
Knauf	1	<i>ref. 36.2</i>	Taxes, Control
<b>AssiDoman</b>	<b>6</b>	<i>ref. 38.2</i>	Ownership

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9a</b>	<b>Second Order Code</b>
Vyborg Paper	3	<i>ref. 39</i>	Ownership, Misimplementation
<b>SBS Agro</b>	<b>4</b>	<i>ref. 40.1</i>	Diversion of Claims
<b>SBS Agro</b>	<b>5</b>	<i>ref. 40.2</i>	Bankruptcy
Inkombank	1	<i>ref. 42</i>	Control
Tokobank	1	<i>ref. 46</i>	Diversion of Claims
Rossiisky Kredit	1	<i>ref. 47</i>	Diversion of Claims
Kosmos TV	1	<i>ref. 49</i>	Control
Channell 5	1	<i>ref. 50</i>	Diversion of Claims
ORT	1	<i>ref. 51.2</i>	Bankruptcy
<b>Subway</b>	<b>7</b>	<i>ref. 52</i>	Control, Diversion of Assets, Ownership
Lomonosov Porcelain Factory	1	<i>ref. 53</i>	Ownership
Kuznetsky Mine	1	<i>ref. 54</i>	Ownership, Misinvestment
MCCI	1	<i>ref. 55</i>	Control, Diversion of Assets, Ownership

According to the reported material, the courts were used with varying degrees of success in 1998. From the review of the litigation category four sub-themes emerged. These sub-themes are government and legislation, ignored court rulings, the role of international courts and finally integrity of formal institutions.

The first sub-theme relates to instances when the courts were used in resolving corporate conflicts with government participation (Rosneft, Gazprom, Transneft, ORT, Krasnoyarsk Hydro Plant and UES). Although the federal government managed to hold its ground in the majority of disputes, there was a clear indication that the judiciary was often at odds with the government's agenda. During a conflict over bankruptcy proceedings against ORT, the court ruled against the company despite its immediate affiliation with president Yeltsin. Eventually, court

marshals were sent to seize the property of ORT in lieu of its debts. Moreover, a number of times the judiciary was used as a tool for reversing transactions that harmed the government's hold over its own assets (Rosneft, UES, Transneft and Krasnoyarsk Hydro Plant, Lebedinsky Ore Mining Plant). The government strongly insisted on legal support that was not always effective and sometimes led to valuable assets being channelled away by unidentified parties (Rosneft, Transneft). Furthermore, inconsistent legislation stemming from political differences between the government and communist-dominated parliament led to contradictory bills that had to be challenged in Constitutional and Supreme courts. Even though the government initiated the suits, analysts expressed uncertainty as to which side the courts would take. This uncertainty was a demonstration of a relative independence of the judiciary from the main power structure (i.e. the government) in the country. A conclusion that the judiciary was independent in 1998 clearly cannot be drawn from this data. However, the fact that the government was often challenged by the judiciary is visible from the analysis of the reported material. In terms of the relationship between local administrations and the judiciary, there were a number of examples suggesting that the local courts were very much under the influence of the former. With reference to Surgutneftegaz, a decision on the ownership of the company's subsidiaries was constantly postponed by St. Petersburg courts. This was in the interest of the local administration which was trying to win control over the assets. In the example featuring Achinsk Alumina Combine, the governor's changing stance on the issue was a key factor in determining decisions of the local courts. Moreover, in the example involving Kuznetsky Mine the foreign investor considered leaving the project because s/he was unable to get anywhere through the local courts which allegedly acted on behalf of the local administration that tried to get control over the recently refurbished factory. The investor concluded that it was impossible to get anywhere if the bureaucrats were not supportive.

Another sub-theme within the perceived environment refers to examples when court rulings were simply ignored. According to the reported material depicting the corporate dispute at Electrosila, a local Financial Industrial Group (EMK) did not respond to a ruling of the court against it. Moreover, analysts suggested that the FIG would prevail in the conflict because it was a large group capable of exerting

pressure on the judiciary. In a more extreme conflict involving Knauf 30 court decisions were ignored by a renegade director who was supported by the local administration.

Separately, there were instances when international courts were used. According to the reported material, this method of dispute resolution was particularly effective when parties to the conflict were financially exposed to the jurisdiction of the selected international court. When Trans World was forced to leave Novolipetsk, the foreign investor won a suit in a Dutch court that ordered the seizure of Novolipetsk's metal in Rotterdam. In cases when there was no proportionate exposure, even when the rulings of international courts were endorsed by both Russian common and supreme courts, the abusing party often managed to prevent official enforcement. In the example involving Subway, the legal challenge was annulled by the fact that the Russian partners re-registered the entity in question using a different name.

Finally, there were a number of positive examples when the courts and other relevant formal institutions were capable of arbitrating and enforcing their decisions. Examples here primarily related to corporate governance violations such as a disputed rights issue (Sibneft), bond issue (Sidanko) and authority of the board (Yukos). The Federal Securities Commission (FSC) was reported as a powerful arbitrator capable of cancelling decisions of the respective boards. Moreover, in a conflict over missing shares of Magnitogorsk, the FSC closed down a local share registrar that authorised deals involving the disputed shares. Furthermore, a Russian court demonstrated its substantial enforcement powers in a conflict when a bank (Rossiisky Kredit) refused to transfer a deposit to its client. After a court ruling in favour of the client, bailiffs seized the property of the bank on behalf of the disadvantaged party. This case showed that the system was in principle capable of meeting the challenges of policing the environment particularly with reference to conflicts where powerful officials did not have personal interests at stake.

In 2006 there were 34 examples<sup>120</sup> of this category reported in the Moscow Times. All of the second order codes were featured in the hierarchy with ownership and diversion of claims disputes being the most widely represented. Graph 4.39 and table 4.28 provide additional information about the category.

Graph 4.39: *Litigation, 2006*

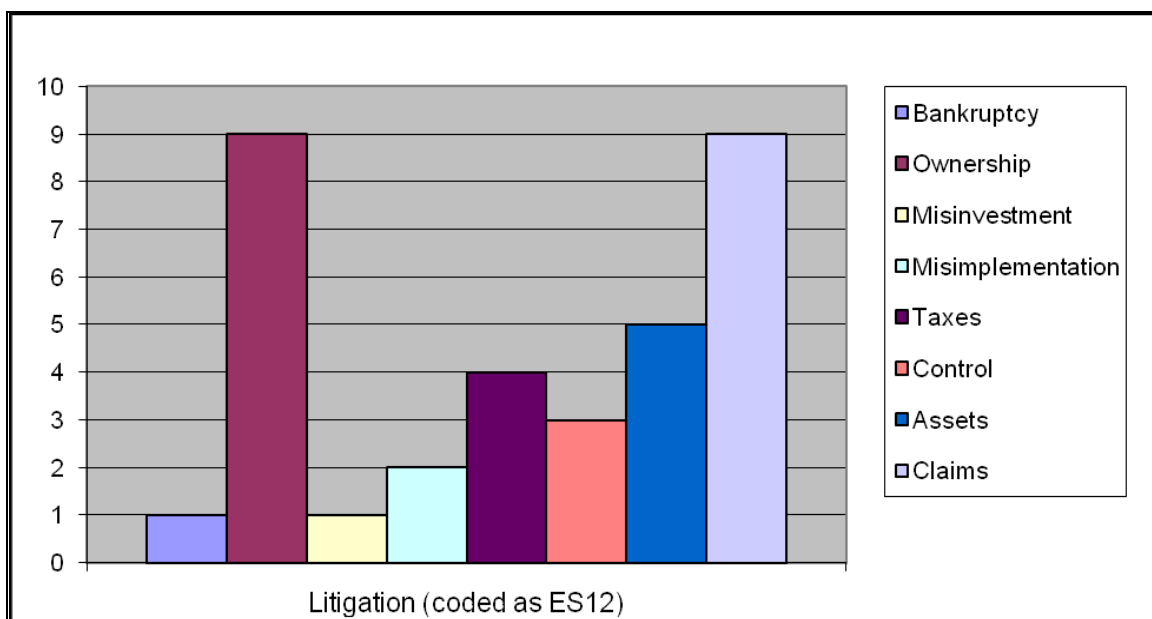


Table 4.28: *Litigation, 2006*

Companies	No of Articles	Reference Appendix 9b	Second Order Code
VimpelCom	1	ref. 4	Misinvestment
MegaFon	2	ref. 5	Diversion of Claims, Ownership
AvtoVaz	2	ref. 6	Control, Taxes
Rosneft	3	ref. 10.2	Diversion of Claims
<b>Rosneft</b>	<b>6</b>	ref. 10.5	Diversion of Claims, Diversion of Assets

<sup>120</sup> 22 separate disputes 12 of which were parallel coded.

<b>Companies</b>	<b>No of Articles</b>	<b>Reference Appendix 9b</b>	<b>Second Order Code</b>
Gazprom	1	<i>ref. 11.1</i>	Ownership
<b>Gazprom</b>	<b>4</b>	<i>ref. 11.3</i>	Diversions of Assets, Ownership
<b>Yukos</b>	<b>23</b>	<i>ref. 12.1</i>	Ownership, Control, Taxes
Yukos	2	<i>ref. 12.2</i>	Diversions of Claims
Yukos	1	<i>ref. 12.3</i>	Diversions of Claims
<b>Yukos</b>	<b>8</b>	<i>ref. 12.4</i>	Bankruptcy
Yukos	1	<i>ref. 12.5</i>	Diversions of Assets
<b>Shell</b>	<b>25</b>	<i>ref. 13</i>	Misimplementation, Ownership, Diversions of Assets
Total	2	<i>ref. 14</i>	Ownership, Diversions of Claims
<b>TNK-BP</b>	<b>15</b>	<i>ref. 16.1</i>	Control, Ownership, Diversions of Assets
TNK-BP	1	<i>ref. 16.2</i>	Taxes
Transneft	2	<i>ref. 18</i>	Ownership
Evraz	1	<i>ref. 31.1</i>	Taxes
RusAl	1	<i>ref. 32.2</i>	Diversions of Claims
RusAl	3	<i>ref. 32.3</i>	Ownership
Eurocement	1	<i>ref. 37</i>	Diversions of Claims
<b>IKEA</b>	<b>4</b>	<i>ref. 48</i>	Diversions of Claims, Misinvestment

In 2006 three main sub-themes emerged from the analysis of the reported material namely international courts, government and legislation, and integrity of formal institutions.

The biggest sub-theme here refers to the role of the state in the court rulings. Previously discussed categories already revealed that in 2006 the Russian government was capable of exerting a great deal of pressure on all institutions in the country. Details of how the government interacted with the judiciary however not only unveiled the extent of this pressure, but also exposed the level of perceived independence of the legal system. All reported cases of corporate disputes falling into this sub-theme showed that the government achieved total control over the legal system. With reference to one of the reported disputes over an ownership stake in a project led by Gazprom, signed agreements specified that all arising conflicts had to be settled in Russian courts only. Analysts suggested that suing the state-owned giant on its own territory was not going to produce any results other than those acceptable to the company and the government. Another example of the state's involvement in the process of formal-dispute resolution was the case involving AvtoVaz when the Prosecutor's General Office suddenly and inexplicably cancelled all criminal challenges allegedly because an agreement was reached with the Russian government. In a society where the judiciary is independent, criminal charges are resolved by the courts and should not be conditioned by non-transparent agreements of the parties instigating the criminal challenge. Disputes involving Yukos, Shell, ExxonMobil, etc. serve as a further demonstration of the prevalence of this perceived characteristic of the Russian judiciary that frequently acts on strict instructions by the government. Additionally, the TNK-BP's example when the company was taken to court for allegedly buying state secrets from government officials further convinced international investors of the level of fabricated regulatory pressure that the government was prepared to resort to while achieving its corporate goals.

With reference to disputes when international courts were referred to for arbitration, in 2006 the Russian state frequently protected itself by arguing a lack of jurisdiction. In a dispute over Yukos, a number of high-ranking Russian officials were served with a US court summons. However, diplomatic immunity and the fact that any rulings had to be endorsed by a Russian court protected the benefiting party (i.e. Rosneft) to the extent that the litigation did not even affect its London Stock Exchange public offering. Similarly, the Russian side argued that the rulings of a US court were inconsequential in a conflict over RusAl's bid for Alcon as the



American court lacked jurisdiction. The bid was blessed by the Russian government and therefore it was suggested that under no circumstances would the Russian courts rule against RusAl even though the company was suspected of severe misconduct. However, the rulings of international courts were not always against the Russian government. A Dutch court ruled in favour of a decision made by a Yukos receiver to fire two directors representing the interests of foreign shareholders. Furthermore, the Russian courts tried to prevent the sale of Yukos' Mazeikiu refinery by declaring it bankrupt. Although Yukos International UK refused to follow the ruling initially, it ultimately complied after a US court returned a similar ruling on the matter.

With reference to the perceived integrity of the Russian court system in conflicts between private parties, powerful associations described in 3.4.4 were still crucially important in navigating a very convoluted and ambiguous court system. The fact that foreign investors of Eurocement were forced to recruit the services of Alfa (a very powerful FIG) suggested that chances of a fair resolution were much higher with a powerful stakeholder on board than without.

In terms of the differences between the two sets of presented data the nature of greater state interference has once again been revealed. It appears that the Russian court system had more authority in 2006 than in 1998 because of the absence of the 'ignored decisions' sub-theme. Unlike in 1998, all court rulings were complied with in relation to corporate disputes reported in 2006. It is difficult to establish whether that would have been the case had the courts returned rulings against the government itself because of the absence of such rulings on Russian soil. Additionally, the intensity of anti-government legal pressure considerably subsided making it difficult to even speculate what the response would have been to such actions in 2006. Conversely, the role of the international judiciary in corporate dispute resolution increased in the more recent year of the study despite its enforcement powers being considerably reduced by the necessity of the Russian courts' endorsement. However, with a greater degree of financial exposure of Russian corporate entities in various jurisdictions, international arbitration should continue to gather momentum.

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## Section 5: Analysis of the Interview Data

In this section corporate disputes mentioned in the interviews will be compared with the coded data. Additionally, the newspaper's independence, accuracy and influence will be discussed.

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### 5.1 Interview Data

In order to test the coded data<sup>121</sup> and determine the newspapers' independence, accuracy and influence, 5 interviews with the Moscow Times reporters have been conducted (chapter 3, sections 2 and 3; the interview guide is presented in appendix 4). With reference to mentioned corporate disputes, the transcripts of these interviews have been compiled into templates based on the same categories that were used in relation to the reported material.

This section of the analysis chapter presents the interview data for the two years examined. For the purposes of triangulation, the coding profiles<sup>122</sup> of all corresponding companies and disputes extracted from the newspaper articles have also been provided.

Additionally, all of the Moscow Times reporters were asked about the paper's independence, accuracy and influence. These questions were designed to analyse possible biases of the reported material as well as comment on the impact that the Moscow Times created in forming investor perception.

The section begins with the analysis of the three interviews with the Moscow Times reporters from 1998 followed by two interviews from 2006. Here, the content is considered with reference to the previously constructed templates. Subsequently, analysis of the Moscow Times reporters' opinion about the newspaper is presented.

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<sup>121</sup> The test needs to establish how fully the constructed templates reflect the reported material of the newspaper.

<sup>122</sup> Templates of the coding profiles are presented in the Appendices 9a and 9b.

## 5.2 Interviews with 1998 Reporters

### Interview 1<sup>123</sup>

During the interview three companies were discussed<sup>124</sup>. Table 4.28 shows the following information:

1. Companies referred to in the discussion;
2. References to the corresponding templates (appendices 9a and 9b);
3. Coding profile of the identified disputes;
4. Number of articles written in connection with each dispute.

Table 4.29: *Coding profiles of companies mentioned during interview No 1, 1998*

Company	Gazprom	Yukos	Parallel Coding	Transneft
Reference	11.4.	12.1.		18.
Coding Profile	<div style="border: 1px solid black; padding: 2px;">           1.1            1.1.2            1.1.2.1            1.1.2.12         </div>	<div style="border: 1px solid black; padding: 2px;">           1.2            1.2.2            1.2.2.1            1.2.2.5            1.2.2.12         </div>	<div style="border: 1px solid black; padding: 2px;">           1.1            1.1.6            1.1.6.1            1.1.6.5            1.1.6.12         </div>	<div style="border: 1px solid black; padding: 2px;">           1.2            1.2.2            1.2.2.2            1.2.2.4            1.2.2.5            1.2.2.7            1.2.2.10            1.2.2.12         </div>
<i>Number of Articles</i>	<b>1</b>	<b>10</b>		<b>7</b>

It is not surprising that it was the biggest companies that the reporter chose to refer to in response to the question about the most representative corporate disputes of the time. Two out of three disputes were extensively covered in the Moscow Times and all of the companies were captured in the coding of the articles.

<sup>123</sup> The interviewee authored a large number of articles particularly with reference to major oil companies. The person was very co-operative and easy to interview. The reporter did not work for the newspaper in 2006. Additional information about the person cannot be revealed due to the guaranteed anonymity and confidentiality.

<sup>124</sup> The companies were mentioned in response to the question about the most representative disputes.

With reference to Gazprom, it was mentioned that the cancellation of the agreement according to which the CEO Rem Vyakhirev managed the government's 35% stake was due to two factors. First, Rem Vyakhirev simply *'fell out of favour with the government'*<sup>125</sup>. Second, minority shareholders tried to stop the transfer of assets from Gazprom to Itera (the largest independent gas producer in the country) that was happening under Vyakhirev. According to the reporter, minority shareholders *"...accused Gazprom of transferring assets to Itera at below market prices or for free..."*<sup>126</sup>. The minority was led by the head of the Federal Securities Commission<sup>127</sup>. Additionally, the pressure on the Chief Executive to leave was further raised by a report compiled by the Audit Chamber that disclosed some *"very damaging information"* about the transfer of assets at Gazprom. However, both the FSC and the Audit Chamber avoided direct accusations and decisive actions because they were *'afraid'* of retaliatory measures from whoever organised the deals. This data confirms the conclusion drawn in the third section of the analysis that in 1998 formal institutions were frequently weaker than unidentified power structures that orchestrated various value-reducing transactions. Moreover, Gazprom's example demonstrated that even the biggest state companies were defenceless against very crude forms of corporate mismanagement.

The second company referred to in the interview was Yukos. The reporter gave the example of transfer pricing that was organised by the parent company Menatep who was poised to dilute holdings of the minority shareholders<sup>128</sup> (including the government)<sup>129</sup>. Table 4.29 shows the coding profile of the dispute which is consistent with the information provided by the reporter. The key concern here was the diversion of claims that minority shareholders loudly protested against *"using both legal suits and PR campaigns"*<sup>130</sup>. The reporter recalled that even though some of the biggest transfer pricing schemes never materialised, the Russian courts consistently ruled in favour of Khodorkovsky (the majority

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<sup>125</sup> Conflict with the State - D1 – 1.1.2.1

<sup>126</sup> Transactions with Self-Interest - D5; this code was not detected through the review of articles.

<sup>127</sup> Litigation - ES12 – 1.1.2.12

<sup>128</sup> Transactions with Self-Interest - D.5 – 1.2.2.5 – 1.1.6.5 (Parallel Coding)

<sup>129</sup> Conflict with the State - D.1 – 1.2.2.1 – 1.1.6.1

<sup>130</sup> Litigation - ES.12 – 1.2.2.12 – 1.1.6.12

shareholder) who was suspected of “*bribing the judges*”. One of the particularly active foreign minority shareholders Kenneth Dart hired a group of lawyers and continuously sued the company for transfer pricing. However, the reporter recalled that the action produced little impact on what the oligarch was doing at the time.

The third company was Transneft. Here the reporter referred to the instance when the management of the company was forced to return a stake that had gone missing further to a questionable consolidation practice (a number of off- shore entities with undisclosed ownership were involved). In addition to the reported material found in the Moscow Times the reporter mentioned the role of tax police<sup>131</sup> that was instrumental in the process of regaining control over the missing stake. Although the template of this dispute does not contain this information, the corresponding third order code (administrative levers of the state) encompasses the practice.

#### Interview 2<sup>132</sup>

In the second interview two companies were discussed in relation to corporate disputes. Similar to interview 1, all mentioned companies and disputes were captured by the coding of the reported material. Table 4.30 shows the coding profile of the two disputes referred to by the second reporter.

Unlike the first interviewee, the second reporter did not refer to the biggest companies, but recalled the most outrageous corporate disputes of the time.

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<sup>131</sup> Taxes - 1.1.6 This second order code was not detected through the review of articles.

<sup>132</sup> Second reporter was also very co-operative and keen to engage in the discussion. The overall impression was that the person was still very much in touch with the corporate life of the country although like reporter number 1 was no longer working for the Moscow Times at the time of the interview.

Table 4.30: *Coding profiles of companies mentioned during interview No 2, 1998*

Company	Sidanko		Knauf	
Reference	22.5	Parallel Coding	36.1	Parallel Coding
Coding Profile	1.1	1.1	1.1	1.1
	1.1.6	1.1.1	1.1.6	1.1.2
	1.1.6.6	1.1.1.6	1.1.6.3	1.1.2.3
	1.1.6.8	1.1.1.8	1.1.6.5	1.1.2.5
	1.1.6.12	1.1.1.12	1.1.6.7	1.1.2.7
			1.1.6.9	1.1.2.9
			1.1.6.10	1.1.2.10
			1.1.6.12	1.1.2.12
Number of Articles	2		1	

The first dispute involved Sidanko’s loss of control over one of its subsidiaries called Chernogorneft. The reporter rather categorically claimed that:

*“...it was Tyumen Oil Co. (TNK) [that] managed to get Chernagorneft from Sidanko in which BP had bought a huge stake and [...] managed, through the bankruptcy courts<sup>133</sup> essentially to steal Chernagorneft out from under Sidanko. It was pretty impressive!”*

This material repeats the coding profile presented on table 4.30. There was an additional point about BP’s incidental participation in the conflict. An interesting point here is that during the interview it was suggested by the reporter that BP paid for its stake in Chernagorneft twice. The first time it paid for it when the British giant bought into Sidanko. The second time it paid for the same asset when much later (2003) it merged with Tyumen Oil Co. to form TNK-BP.

Furthermore, the reporter elaborated on the way the bankruptcy law was used in the dispute:

*“... you had to come up with some overdue debts and the way the bankruptcy law worked at the time was [that] if you had those [debts] you could declare the company bankrupt. Then you have the Creditors’ Committee and if you’re the first in line [if you’re the biggest in the Creditors’ Committee] then you could essentially get control of the company.”*

<sup>133</sup> Bankruptcy - 1.1.1 and Control - 1.1.6 (Parallel Coding).

Both points were covered in the published material of the newspaper. However, the reporter resorted to much stronger language in the interview than the terms used in the corresponding articles. Similar to interview 1, the corrupt role of the Russian judiciary was discussed<sup>134</sup>. It was suggested that Tyumen<sup>135</sup> was able to manipulate the court system and got favourable rulings because at the time the judges were “*inexperienced and underpaid*”.

The second dispute that the reporter referred to was Knauf. This dispute was constantly featured in the analysis of the coded material and arguably was the most shocking example of corporate battles for control and ownership reported by the newspaper in 1998. In order to illustrate the point and demonstrate consistency with the coding (table 4.30) the following extract from the interview has been selected:

*“...essentially this German company called Knauf, a building materials company, had bought a controlling stake in the factory<sup>136</sup>. They were concerned about the director they thought he was stealing from them<sup>137</sup>, – and so they decided to try to get rid of him. The director had the administrative resource i.e. he knew the head of the local administration very well and he had good connections with the local Cossacks<sup>138</sup>. So Cossacks – and I’m talking full-on Cossacks with the hats, the capes, on horses and with swords actually besieged the factory supporting the director’s interests<sup>139</sup>. By the time I got there a lot of the Cossacks were gone but each side had their huge security forces – there were two separate security forces in the building and there were more security people than there were executives of any kind. The Germans were hauled up in one of the rooms in the administrative building, their electricity had been cut off, they had a generator and a satellite fax and they were sending faxes to Moscow saying help us... [and] what do we do<sup>140</sup>? Anyhow it was one of those typical situations where I think the factory already had two boards of directors<sup>141</sup>. The renegade director had chosen his board of directors and the Germans had their board of directors...<sup>142</sup> [The situation] didn’t get resolved at the administration level; I mean the*

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<sup>134</sup> Litigation - ES.12

<sup>135</sup> Third-Party Enforcement - ES.8

<sup>136</sup> Ownership - 1.1.2 and Control - 1.1.6 (Parallel Coding)

<sup>137</sup> Transactions with Self-Interest - D.5

<sup>138</sup> Administrative Levers of the State - ES.10

<sup>139</sup> Private Enforcement - ES.6

<sup>140</sup> Self-Enforcement - ES.7

<sup>141</sup> Control - 1.1.6

<sup>142</sup> General Meetings - D.3

*administration was on the director's side and was demanding that the Germans give back 25% of the shares that they had bought ... The administration said "Give us back 25%" and, we'll solve this problem ... [The situation] was ultimately resolved at the level of a meeting between Yeltsin and Cole. It was just impossible to resolve it at any level other than that."*

Besides demonstrating that the coding profile and the corresponding template (ref. 36.1) match the reporter's account, the narrative also suggests that it was a typical situation at the time. This is consistent with the content of the second order codes associated with the control and ownership categories where the analysis revealed a number of instances involving renegade directors and examples of corporate insubordination.

### Interview 3<sup>143</sup>

The third and final reporter from 1998 mentioned three companies: Yukos, Norilsk Nickel and AvtoVaz (manufacturer of Lada cars). Again, all of the companies and related disputes were captured in the coding.

Table 4.31: *Coding profiles of companies mentioned during interview No 3, 1998*

Company	AvtoVaz	Yukos	Parallel Coding	Norilsk Nickel
Reference	6	12.1.		28.1
Coding Profile	1.2 1.2.2 1.2.2.5 1.2.2.9	1.2 1.2.2 1.2.2.5 1.2.2.1 1.2.2.12	1.1 1.1.6 1.1.6.5 1.1.6.1 1.1.6.12	1.1 1.1.2 1.1.2.5 1.1.2.10 1.1.2.12
Number of Articles	1	10		1

As far as the previously mentioned dispute involving Yukos was concerned, the information recalled by the reporter was identical to what was discussed in the first interview. However, the fact that this dispute keeps being mentioned is indicative of its importance in forming investor perception. Once again independence of the

<sup>143</sup> The third reporter stopped working for the newspaper a considerable time ago and struggled the most remembering facts about corporate disputes.



judiciary was in question and the unchallenged powers of the oligarchs were acknowledged<sup>144</sup>. The reporter also reverted to a considerably stronger language than that used in the articles. It was suggested that the oligarchs at the time could “*do anything they wanted*” particularly when it came to violating rights of minority shareholders<sup>145</sup>. Even though the reporter pointed out that one of the affected shareholders (Kenneth Dart) was very experienced at fighting share dilution, numerous court cases were still inconsequential in the fight against oligarchs who were very much above the law. An additional point with reference to this particular conflict was that the reporter came across a number of instances when “*minority shareholders were intimidated by Menatep and Khodorkovsky in particular to the extent that legal challenges were simply dropped*”. This is a confirmation of the applicability of the private enforcement category with reference to the way Yukos was managed in 1998<sup>146</sup>.

The second company mentioned during the interview with the third reporter was AvtoVaz. The reporter recollected the role of severely corrupt dealerships who charged abnormally high prices for their services. This information was also included in the corresponding template as demonstrated in the coding profile presented in table 4.31. An additional point with reference to this conflict however was the fact that the problem of corrupt dealerships was confined to AvtoVaz and was not necessarily applicable to other car manufacturers some of which were fairly well run (e.g. Gaz, the second largest producer of cars in the country).

Finally, Norilsk Nickel was discussed by the reporter. The dispute was partially instigated by a report produced by the Audit Chamber that in general was extremely critical of the loan-for-shares deals. Even though the reporter suggested that the chances of re-nationalisation were extremely slim, uncomfortable questions were still asked about how major assets ended up in the hands of so few oligarchs.

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<sup>144</sup> Litigation - ES.12

<sup>145</sup> Transactions with Self-Interest - D.5

<sup>146</sup> Private Enforcement - ES9; although this category was not detected with reference to this particular dispute the use of private enforcement was registered with reference to the company (see template 12.7).

Examples of the 1998 disputes mentioned by the reporters not only complement the data and corresponding codes, but more importantly confirm the fact that no major disputes have been omitted from the analysis of the reported material. In total, two additional codes were revealed through the analysis of the interview transcripts that were not detected during the main stage of data analysis (Gazprom - D5 and Transneft - Taxes). These codes were not included in the general coding profiles because the corresponding information was never reported and hence did not have such an impact on investor perception<sup>147</sup>. Nevertheless, it is still important to note that these codes add to the accuracy of representation of the actual disputes. Hence, the additional codes revealed by the interviews are a good measure of the limitations of this study. In this context the limitations refer to the extent to which the reported material reflects actual events<sup>148</sup>.

### 5.3 Interviews with 2006 Reporters

Two reporters who worked for the Moscow Times in 2006 were interviewed. These interviews were more fruitful simply because of the proximity to the events with some of the mentioned disputes still being resolved at the time of the interviews. In this context there was an inevitable overlap with some of the facts pertaining to 2007 (the year when the interviews were conducted).

#### Interview 1<sup>149</sup>

In answer to the question about the most representative disputes the first reporter referred to two companies which were Rosneft and Yukos. Below are the coding profiles of the conflicts in question.

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<sup>147</sup> To make sure that this was the case reported material was scanned again.

<sup>148</sup> Out of 35 codes used to describe the 7 chosen disputes, omission of 2 additional codes does not seem damaging particularly in the context of the complexity and size of the data set.

<sup>149</sup> The interviewed reporter did not work for the newspaper at the time of the interview. The person was very opinionated about the Russian government's approach to dealing with international oil companies.

Table 4.32: *Coding profiles of the companies mentioned during interview No 1, 2006*

Company	Rosneft		Yukos		
Reference	10.5	Parallel Coding	12.1	Parallel Coding	Parallel Coding
Coding Profile	1.2	1.2	1.1	1.1	1.1
	1.2.2	1.2.1	1.1.2	1.1.6	1.1.5
	1.2.2.5	1.2.1.5	1.1.2.1	1.1.6.1	1.1.5.1
	1.2.2.6	1.2.1.6	1.1.2.5	1.1.6.5	1.1.5.5
	1.2.2.10	1.2.1.10	1.1.2.9	1.1.6.9	1.1.5.9
	1.2.2.12	1.2.1.12	1.1.2.10	1.1.6.10	1.1.5.10
			1.1.2.12	1.1.6.12	1.1.5.12
<i>Number of Articles</i>	6		23		

The reporter chose to discuss the most talked-about dispute of the year 2006 and possibly in the modern history of corporate Russia – re-nationalisation of Yukos. As demonstrated by the number of articles published in the Moscow Times, the way this conflict was handled by the Russian authorities created a very strong impact on the perception of foreign investors about the realities of doing business in the country.

As opposed to 1998 accounts, the interviewed reporter presented Khodorkovsky (former Chief executive of Yukos) in very favourable terms. The reporter’s view was completely anti-government with allegations such as ‘... *[it] was the legitimate political ambitions of Khodorkovsky that led to his arrest*’. The fact of fabricated back taxes was also acknowledged:

*“... Yukos was the biggest Russian oil company where the management was very capable and ran the company better than its competitors. It is difficult to see how this company could suddenly accumulate such a massive [back] tax liability, particularly remembering the fact that its accounts had been publicly audited.”*

The reporter defended Khodorkovsky along with the actions of other primarily foreign shareholders who attempted to sue the government in various international courts. A great deal was mentioned about the way the Russian government used the tax authorities<sup>150</sup> in the pursuit of the assets and the FSB in the tasks of

<sup>150</sup> Taxes - 1.1.5, Control - 1.1.6, Ownership - 1.1.2 (Parallel Coding)

silencing Russian lawyers through practices like beatings, unlawful jailing as well as unjustified extraditions in relation to foreign lawyers<sup>151</sup>. In terms of the benefiting parties it was suggested that the actions were probably initiated by “... *one or two individuals on the board of directors [of Rosneft] who were known for their readiness to resort to some sort of assistance from the Federal Security Bureau*”. These people were very firmly set in the Russian government and sometimes are referred to as ‘siloviki’ (the Russian word for force). In many ways the opinion of the reporter was fairly one-sided. This fact was ultimately reflected in the published material and consequently influenced the template of the dispute (12.1).

The reporter went on to discuss the second company Rosneft. It was very clearly suggested that the London IPO of the company was “... *equivalent to the international acceptance of the re-nationalisation [of Yukos] that Rosneft was the sole beneficiary of*”. It was suggested that Rosneft’s assets, a large proportion of which previously belonged to Yukos, were legitimised by the sale of its shares on the London Stock Exchange. The reporter also mentioned the “*relationship building exercise*” that international oil companies like BP were keen to engage in by buying a stake in Rosneft. It was mentioned that the investment was not of a commercial charter, but an opportunity for the British company to display its loyalty to the Russian government<sup>152</sup>.

With reference to the two disputes, the information disclosed by the reporter was very consistent with the constructed templates that encompassed all of the discussed material.

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<sup>151</sup> ES.9 - Private Enforcement

<sup>152</sup> ES.6 - Relationship-Based Enforcement

## Interview 2<sup>153</sup>

The second interviewee mentioned Gazprom, Shell, TNK-BP and a small company that was not featured in the Moscow Times reports<sup>154</sup>. Table 4.33 provides the coding profiles and references to the corresponding templates in relation to the three disputes mentioned in the second interview.

Table 4.33: *Coding profiles of the companies mentioned during interview No 2, 2006*

Company	Gazprom			Shell			TNK-BP		
Reference	11.3	Parallel Coding	13	Parallel Coding	Parallel Coding	16.1	Parallel Coding	Parallel Coding	
Coding Profile	1.2	1.1	1.1	1.1	1.2	1.1	1.1	1.2	
	1.2.1	1.1.2	1.1.4	1.1.2	1.2.1	1.1.6	1.1.2	1.2.1	
	1.2.1.1	1.1.2.1	1.1.4.1	1.1.2.1	1.2.1.1	1.1.6.1	1.1.2.1	1.2.1.1	
	1.2.1.4	1.1.2.4	1.1.4.10	1.1.2.10	1.2.1.10	1.1.6.6	1.1.2.6	1.2.1.6	
	1.2.1.10	1.1.2.10	1.1.4.11	1.1.2.11	1.2.1.11	1.1.6.9	1.1.2.9	1.2.1.9	
	1.2.1.12	1.1.2.12	1.1.4.12	1.1.2.12	1.2.1.12	1.1.6.10	1.1.2.10	1.2.1.10	
						1.1.6.11	1.1.2.11	1.2.1.11	
						1.1.6.12	1.1.2.12	1.2.1.12	
<i>Number of Articles</i>	<b>4</b>		<b>25</b>			<b>15</b>			

During the interview all of the mentioned disputes were discussed in the context of the government assisted takeovers by state owned companies like Gazprom.

With reference to the gas producer it was noted that the company was the main beneficiary further to the redistribution of assets that previously belonged to Shell and TNK-BP. However, unlike Rosneft, the key decision makers in Gazprom did not resort to the ‘services’ of the FSB. Here, “... *the preferred tool was the false environmental charges*” that were used in order to build up pressure until the companies in question were prepared to concede control for an acceptable price. The difference in approaches meant that there was no unified practice in determining the way state companies went about re-gaining control over strategic assets. To a large degree, it was the personalities of the chairmen and CEOs of

<sup>153</sup> The reporter continued working for the Moscow Times at the time of the interview which possibly made the person refer to some of the events that took place after 2006. The reporter was also very outspoken about the role of the Russian government in corporate affairs.

<sup>154</sup> The reason the small factory outside Moscow was used as an example was because the reporter knew the owner and the director of the company personally.

Gazprom (more liberal) and Rosneft ('siloviki' or force) that determined the nature of attacks on companies like Shell and TNK-BP. In addition, the fact that in 2006 the Russian government enforced policies through practice and not laws was also mentioned during the interview: "... *the bill on investments in strategic sectors did not get released until much later meaning that companies like Shell, who admittedly purchased their stakes very cheaply in the chaotic environment of the 1990s, had no idea about what was coming*"<sup>155</sup>.

Consistent with the coding profile of Shell the reporter suggested that the company could have foreseen the situation and pro-actively invited Gazprom into its Sakhalin 2 project. It was suggested that if that had been done, then the company would not have experienced the same amount of pressure from the environmental agencies and consequently would have been in a better position to ask for more money from Gazprom<sup>156</sup>. Instead Shell announced a \$10 billion cost increase which meant that the government had to wait longer before it got its share of the profits (terms of the Production Sharing Agreement). In this respect, the management of Shell made an incorrect assumption that the government would do nothing about it. Conversely, the government reacted "... *swiftly and decisively by instructing Gazprom to take over the asset, which in turn relied on the Natural Resources Ministry that manufactured false environmental allegations*".

With reference to TNK-BP, in principle, the same situation was described with the difference that it was Rosneft behind the mounting pressure on the company. Consequently, '*... because it was Rosneft's officials masterminding the attacks on the company, alternative agencies and tools were employed.*' In particular, the use of the Prosecutor General's Office was emphasised giving rise to speculations of their close connections with Rosneft's chairman, Igor Sechin. Although the TNK-BP template does not reveal this connection, it nevertheless captured the fact that the Prosecutor General's Office was instrumental in this particular conflict. Additionally, the interviewee referred to the situation where BP and TNK-BP foreign employees suddenly started having problems with renewing their Russian

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<sup>155</sup> Unclear Rules - D.4

<sup>156</sup> Misimplementation - 1.1.3

visas. This fact coincided with the company's problems with Rosneft and Gazprom. In this regard it was noted that:

*"... all foreign employees in Russia break immigration rules to some degree because it is simply impossible to adhere to them. In general, this is not a problem because nobody pays any attention to that fact. However, if you suddenly fall out of favour with the government, it is just another weapon they have against you."<sup>157</sup>*

This fact was not captured by the coding because it referred to the continuation of the dispute that was reported later in 2007 (a year not covered by the study). Nevertheless, this is very illustrative of the way foreign investors perceived the environment because the issue at hand affected all of them who entered the country at least once. Lastly, an example of a small manufacturing company was used to further confirm the preferred practice of dealing with unwanted investors. It was claimed that:

*"... any private entrepreneur has to bribe officials at every level to get things done. But the real problem with this is that when you suddenly fall out of favour, you have no legal foundation at all. So ... the real choice is either get completely tangled in endless and meaningless bureaucracy or become part of the corrupt system."*

The point here is that by becoming part of the system foreign entrepreneurs lose all means of formal protection and become more vulnerable.

In general, the presented analysis of the transcripts confirmed the accuracy and consistency of the constructed templates. With reference to 1998 and 2006, all mentioned disputes (apart from one) were coded and no interviewee revealed any information that contradicted the content of the respective templates and codes. The fact that the smaller dispute referred to by a 2006 reporter was not found in the templates reflects the tendency of the newspaper to publish material about larger entities. However, in terms of this research it is not a problem because the focus of the study is on the perception of the key features of the respective environments that, as it happens, are best described by the events involving larger companies.

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<sup>157</sup> Unclear Rules - D.4

## 5.4 Independence, Accuracy and Influence of the Moscow Times

### - Independence

One of the key concerns about the data set was the fact that the reported material was subject to external influences that distorted the reported material. For example, in 2006 there was a great deal of concern over the whole concept of the freedom of speech in the Russian context. In order to understand how these external forces affected the Moscow Times reporting and hence the data, all interviewed reporters were asked the question about the newspapers' independence. Analysis of reporters' answers revealed that there were no concerns over the freedom of speech with reference to the newspaper. Both 1998 and 2006 reporters made it clear that the Moscow Times did not experience any political pressure due to the relatively small number of Russian readers. The following quotes illustrate the point:

*"... the readership of the newspaper is not big enough to be on the Kremlin's radar and therefore its reporting is free from political pressure, which most Russian language newspapers have to deal with."*

*"I don't think that the Moscow Times was ever really hugely influential inside of Russia, I don't think that the Kremlin really paid it much attention frankly and I doubt that it does today either... I don't get the sense that it was never under huge pressure politically from the Kremlin, just because they never saw it as important, really."*

A reporter who worked for the newspaper in 1998 pointed out that at some stage in the 1990s, Khodorkovsky (CEO of Yukos) bought a stake in Independent Media, the company that owns the Moscow Times. One of the promises that he made prior to the purchase was that he would not interfere in the editorial. But the reporter claimed that the promise was broken when on a number of occasions Khodorkovsky tried to exert influence<sup>158</sup> about the way Yukos was presented in the newspaper. However, '*... by 1998 Khodorkovsky stopped interfering because he had more important things to do like dealing with the financial crisis that hit his company and the country*'. In any case, the reporter added that this fact

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<sup>158</sup> The reporter suggested that Independent Media was raided by the tax police at Khodorkovsky's request.



did not have a significant influence on the newspaper's coverage of events, even in connection with Yukos (in the 1990s the newspaper was fairly critical of the way the company treated minority shareholders). Similarly, a reporter who worked for the newspaper in 2006 admitted that occasionally they received letters from companies like Gazprom and Rosneft about particularly critical articles. However, the reporter said that those letters had a non-threatening tone and simply asked for an explanation about why certain things had been written, rather than sought to warn or deter reporters from openly criticising the companies. The reporter also suggested that the Moscow Times was never under the same pressure as its Russian counterparts where reporters were intimidated, and in the worst cases even assassinated for their coverage.

- Accuracy

In terms of the accuracy of the reported material the previously discussed bias in favour of foreign investors was unanimously acknowledged by all interviewed reporters. The bias was determined by two facts. First, the newspaper's targeted readership was foreigners living and working in Russia. Second, foreign minority shareholders were much more prepared to talk to the reporters than Russian officials who frequently were simply inaccessible. Although all of the reporters said that they made an effort to get the Russian side to talk<sup>159</sup>, interviews were often very difficult to arrange because of the secretive culture of Russian companies.

- Influence

Finally, according to the interviewed reporters, the Moscow Times coverage was an influential factor in determining investor perception about the environment. As one of the reporters pointed out:

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<sup>159</sup> When the reporters did manage to arrange interviews with Russian managers, often the content was very superficial. Additionally, during the course of most of the interviews it emerged that the reporters interviewed Russian managers in Russian. Clearly, this is partially an explanation of the pro-western bias because, in general, for the reporters, it is much easier to talk in their native language (which with reference to all interviewed reporters was English).

*“... [the newspaper] was very influential among foreigners who worked in Russia because it was the only thing many of them could read so I once saw Condoleezza Rice with it under her arm and I saw John Bolton carrying it around his hotel so it was influential with US politicians and business people.”*

Moreover, another reporter said that the newspaper shaped investor perception beyond its direct readership:

*‘The Moscow Times coverage was very important for foreign perception; first of all the foreigners in Moscow read it and the people who were interested in Russia read it and it had an influence on all the foreign correspondence in Moscow so what the Moscow Times wrote influenced what the New York Times wrote. I know plenty of cases where ... the correspondents working for the foreign papers would pick up on stories that were first reported in the Moscow Times including the Economist.’*

In conclusion, the analysed interview data demonstrated/confirmed that the constructed templates:

5. Adequately reflect the reported material of the newspaper (i.e. no major disputes were omitted from the coded material);
6. Are based on the reports which were largely independent, accurate (although biased in favour of foreign investors) and influential in terms of forming investor perception.

## Chapter Summary

This chapter presented the numerical overview of coded data, followed by a detailed analysis of the content of second- and third-order codes. With reference to each code, key comparisons were made between the two years of the study. Each time a code was introduced a graphical representation was included in order to depict the extent of coverage provided by the newspaper. The content of all second-order codes was included in the analysis whereas the third-order codes were presented together with references to the corresponding templates.

The final section of the chapter presented the interview material, analysis of which, helped to triangulate the coded data. It was demonstrated that every possible precaution was taken in order to ensure that no major disputes were missing out from the coded data and consequently analysis.

The analysis of the codes and their content revealed a number of changes in the institutional environment in Russia. The following chapter is designed to present these changes with reference to each code.

## CHAPTER 5: FINDINGS AND DISCUSSION

### 5.1 Introduction

Chapter 4 demonstrated how the collected data set (appendices 9a and 9b) was transformed into information about institutional change in Russian corporate governance based on the two time periods. The key objective of this chapter is to present that information in a structured way with a link to the relevant literature. This chapter concludes with a detailed outline of the original contribution of the study.

### 5.2 Framework for Presenting the Findings

Because of the high level of detail and complexity of the analysis, it is important to ensure that the findings are presented in a structured way. In order to make the overall comparison possible, the findings about the registered change in perception of the environment in Russia will be divided into two groups:

- Forces that stimulate the improvement of corporate governance
- Forces that prevent the development of corporate governance.

The findings presented in table 5.1 need to be considered in conjunction with the framework (chapter 2, figure 2.3) that was created at the stage of the literature review. The purpose of the framework is to summarise the key drivers in the process of institutional evolution in the context of Russian corporate governance. The table shows all used codes, corresponding forces and additional references to related codes (necessary because of parallel coding).

Table 5.1: *Forces that determine institutional change in Russian corporate governance.*

Coding	Forces that stimulate improvement of corporate governance	Forces that prevent the development of corporate governance
Bankruptcy 1.1.1	<ul style="list-style-type: none"> <li>• Formal institutions have accumulated much greater enforcement powers capable of confronting even the most powerful oligarchs</li> <li>• Protection of unviable businesses has subsided</li> <li>• Bankruptcies have stopped being used by private groups as a mechanism for seizing control; reference: 1.1.6.</li> </ul>	<ul style="list-style-type: none"> <li>• A precedent has been set when bankruptcy proceedings were used to destroy a financially viable entity for political reasons; reference: 1.1.2, 1.1.6, 1.2.1, D.1, D5, ES.10.</li> </ul>
Ownership 1.1.2	<ul style="list-style-type: none"> <li>• Property rights have become stronger in conflicts without state involvement</li> <li>• Private ownership has become more transparent; reference: D.2.</li> </ul>	<ul style="list-style-type: none"> <li>• Politically motivated re-allocation of property has gathered momentum; reference: 1.2.1, D.1, D.5, ES.10.</li> </ul>
Misinvestment 1.1.3	<ul style="list-style-type: none"> <li>• Shareholders have begun to challenge investment projects more effectively; reference: D.3.</li> </ul>	
Misimplementation 1.1.4		<ul style="list-style-type: none"> <li>• Implementation of viable investment project has become more difficult due to increased government interference; reference: D.1, ES.10.</li> </ul>

Coding	Forces that stimulate improvement of corporate governance	Forces that prevent the development of corporate governance
Taxes 1.1.5	<ul style="list-style-type: none"> <li>Emergency tax collection has become less of a feature of the environment</li> <li>Tax authorities have stopped acting on behalf of self-centred private individuals; reference: 1.1.2, 1.1.6, D.5.</li> </ul>	<ul style="list-style-type: none"> <li>Tax authorities have become instrumental in the political re-distribution of property; reference: 1.1.2, 1.1.6, D.1, D.5, ES.10.</li> </ul>
Control 1.1.6	<ul style="list-style-type: none"> <li>Legitimate shareholders have a greater level of control over private corporate entities which do not attract the attention of the state</li> <li>Culturally, there is a greater level of acceptance of authority of private owners; reference: 1.1.2.</li> </ul>	<ul style="list-style-type: none"> <li>There has been complete lack of regard for legitimate owners' authority when the government was involved in corporate disputes; reference: D.1, ES.10.</li> </ul>
Diversion of Assets 1.2.1	<ul style="list-style-type: none"> <li>Private companies in need of foreign finance have become more pressured to price their assets according to the market value.</li> </ul>	<ul style="list-style-type: none"> <li>Acquisitions of valuable assets by state companies have not followed market rules; reference: D.1, ES.10.</li> </ul>
Diversion of Claims 1.2.2	<ul style="list-style-type: none"> <li>Private companies have improved their corporate image by not engaging in the practice of blatant expropriation; reference: D.5.</li> </ul>	<ul style="list-style-type: none"> <li>The government has engaged in the most daring expropriation of assets reference: D.1., D.5, ES.10.</li> </ul>
State Interference D.1		<ul style="list-style-type: none"> <li>The government has become much more aggressive and capable of regaining control and ownership over key assets (re-nationalisation) despite existing agreements and contracts; reference: 1.1.2, 1.1.6, D.5, ES.10.</li> </ul>

Coding	Forces that stimulate improvement of corporate governance	Forces that prevent the development of corporate governance
Inadequate Information D.2	<ul style="list-style-type: none"> <li>• Ultimate beneficiaries have started the trend of disclosing their holdings; reference: 1.1.2.</li> </ul>	<ul style="list-style-type: none"> <li>• The environment continues being filled with secretive entities with undisclosed ownership and unaudited financial information</li> <li>• Shareholders continue to receive confusing and misleading information ahead of important votes.</li> </ul>
General Meetings D.3	<ul style="list-style-type: none"> <li>• Blatant abuse of voting rights and illegal resolutions have become less prominent</li> <li>• Confidence in the adequacy of board representation has increased<sup>160</sup>.</li> </ul>	
Unclear Rules D.4	<ul style="list-style-type: none"> <li>• Clarity of rules and laws has increased.</li> </ul>	<ul style="list-style-type: none"> <li>• Corporate raids continue to be made possible by existence of laws which are impossible to follow; reference: 1.1.2;</li> <li>• The government has been enforcing policies based on practice and not laws; reference: 1.1.2, 1.1.6, D.1, D.5, ES.10, ES.12.</li> </ul>
Transactions with Self-Interest D.5	<ul style="list-style-type: none"> <li>• Self-centred actions initiated by private owners have become less visible.</li> </ul>	<ul style="list-style-type: none"> <li>• Massive self-centred dealings continue to be a feature of non-transparent state companies; reference: D.2.</li> </ul>
Relationship-Based Enforcement ES.1	<ul style="list-style-type: none"> <li>• Non-transparent out-of-court settlements have become a less prominent feature of the environment; reference: D.2.</li> </ul>	<ul style="list-style-type: none"> <li>• Corporate cronyism has elevated itself to the institutional level.</li> </ul>

<sup>160</sup> Previously, ownership did not necessarily translate into proportionate board representation and voting rights.

Coding	Forces that stimulate improvement of corporate governance	Forces that prevent the development of corporate governance
Self-Enforcement ES.2	<ul style="list-style-type: none"> <li>• Barbarian corporate behaviour initiated by private parties has subsided in prominence; reference: 1.1.2, 1.1.6, D.5;</li> <li>• Unions have stopped being abused in corporate conflicts</li> <li>• The process of dispute resolution has generally become more sophisticated.</li> </ul>	<ul style="list-style-type: none"> <li>• Financial Industrial Groups continue to be powerful arbitrators in the environment</li> <li>• Anonymous power structures continue to be active in the environment; reference: D.2.</li> </ul>
Third-party Enforcement ES.3	<ul style="list-style-type: none"> <li>• Finance providers have begun to act as important enforcers of good corporate governance standards.</li> </ul>	<ul style="list-style-type: none"> <li>• Financial Industrial Groups continue to be powerful arbitrators in the environment</li> <li>• Anonymous power structures continue to be active in the environment; reference: D.2.</li> </ul>
Private Enforcement ES.4		<ul style="list-style-type: none"> <li>• Corporate violence has not subsided, and now radiates from the establishment rather than private individuals; reference: ES.10.</li> </ul>
Administrative Levers of the State ES.5		<ul style="list-style-type: none"> <li>• The level of centralised state command of its own ministries and institutions has grown considerably.</li> </ul>
Shadow of Enforcement ES.6		<ul style="list-style-type: none"> <li>• Greater capacity of the state has begun to act as a stronger deterrent of corporate actions against the government.</li> </ul>
Litigation ES.7	<ul style="list-style-type: none"> <li>• International arbitration has gathered momentum</li> <li>• Courts have begun to be taken more seriously.</li> </ul>	<ul style="list-style-type: none"> <li>• The state continues to exert a lot of influence over all levels of judiciary in the country.</li> </ul>



It is important to reiterate that the above statements correspond to key drivers which determine the change in the institutional make-up of the country in perceived terms. Although they appear to be real factors illustrating the evolutionary process of Russian governance there is an important limitation that refers to the capacity of the newspaper to reflect the actual situation.

With reference to figure 2.1 (chapter 2), the presented material adds to the understanding of the dynamics of the institutional change in the country. Some of the forces identified in the figure are not consistent with the content of table 5.1. The inconsistencies primarily relate to the role of the state in ensuring a general trend towards the rule of law in the country.

### **5.3 Institutional Change in Russian Corporate Governance**

From the presented findings, an important distinction needs to be drawn. A meaningful discussion of the institutional change in Russian corporate governance has to distinguish between state companies and private entities and shareholders.

#### **5.3.1 Institutional Change in Russian Corporate Governance: The Role of the State**

According to the detailed analysis of corporate conflicts, there appears to have been a significant deterioration in the perception of the institutional environment in Russia. This perceived deterioration manifested itself through a number of factors that refer to 2006 and were not as prevalent in 1998. These factors are:

- The policy of widespread re-nationalisation of key strategic assets into the hands of non-transparent entities
- A court system which is subordinate to the administrative elite<sup>161</sup>

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<sup>161</sup> Frequently, self-centred actions are sold to the public as a coherent political agenda with national interests in mind.

- Governmental agencies and ministries that resort to selective sanctioning in resolving important corporate conflicts
- Culture of extra-judiciary involvement originating from the government.

Additionally, the following negative features of the environment were detected in both years of the study:

- Low level of observance of formal agreements and contracts;
- Weak markets incapable of dictating terms of major transactions;
- Culture of corporate cronyism within the government;
- Administrative elite which consists of self-centred individuals;
- Artificially created bureaucratic hurdles that are designed to act as 'gate-keepers' for the government officials.

In terms of the moderately positive changes in 2006, the Russian government:

- Increased its capacity to regulate the environment;
- Increased its financial stability and independence;
- Increased control over local administrations and competing power structures.

The above findings demonstrate that the increased capacity of the state contributed a great deal to the deterioration of the perceived integrity of the institutional environment in the country. This is in contrast to Gel'man (2004) and Kuznetsov & Kuznetsova (2003) who suggested that a stronger state should lead to a diminishing power of informal institutions. On the contrary, in the Russian context the increased capacity of the state (in the short to medium term) has led to the incorporation of previously autonomous informal networks into the establishment. The latter has begun to rely on extra-judiciary enforcement in the instances where formal arbitration does not produce the desired (by the government) effects. The coded material reveals evidence that on the level of perception, this fact has led to a further entrenchment of informal institutions which

started to function as an executive arm of the enforcement machinery of the state. Put differently, in the Russian context, it is not about the contradiction between informal power structures and the state, but the state seeking to co-operate with the informal institutions in the quest for a greater level of control over commercial activities in the country.

Therefore, the growing capacity and power of the government are being perceived as a threat to the desired development of a predictable regulatory infrastructure (i.e. formal institutions). In this sense, the expected change toward a more developed culture of market control is unlikely to be perceived as a feasible outcome of the ongoing trend. This is an important addition to Roberts' (2004) findings who predicted an improvement of corporate conduct once companies become exposed to international markets. The coded data suggests that with reference to state companies, the latter proposition needs to be treated with additional caution.

Furthermore, the concept of 'administrative government' (Pistor & Xu, 2005) has discredited itself to the extent that it cannot be perceived as a viable alternative to legal governance in the Russian context. Moreover, the coded data suggests that the frequently cited proposition that it is the incomplete laws in Russia that have hindered the development of capital markets (Pistor & Xu, 2005) does not hold true from the perspective of the state companies. In terms of perception, the analysed data suggests that even if all the required laws were in place, the culture of the Russian administration does not preclude the use of various administrative techniques that inhibit justice and hence destroy confidence in the capital markets. In this regard, the data supports Black's (2001) proposition that it is the fact of inferior enforcement that constitutes the central problem for the Russian corporate governance. However, this study emphasises the destructive role of the state in the latter proposition and predicts further deterioration of the sentiment in relation to the development of capital markets in the country. In other words the consequences of the corrupt government described by Black, Kraakman & Tarassova (2000) are coming into fruition in the context of its extended financial power and control. Furthermore, it is irrelevant to discuss the progress of corporate governance reforms until formal institutions such as the courts and

market regulators acquire sufficient integrity to challenge the state. The analysed data suggests that, in perceived terms, the opposite is happening in Russia.

Moreover, to a limited degree this phenomenon of the Russian corporate environment has been exported (alongside billions of barrels of oil) to even some of the most established international markets, where investment decisions (for example Rosneft's listing on the London Stock Exchange) were made on the basis of political manoeuvring rather than in the commercial interests of the shareholders. In this context, contrary to Roberts (2004), it is possible to suggest that the international capital markets may be negatively affected by the strong presence of Russian state companies. This is particularly true for the state monopolies from strategic sectors that together with their substantial resources impose political bargaining and, in general, inferior corporate culture.

It is also important to acknowledge that the system is very inert and is unlikely to change drastically due to the strong presence of cronyism within the government. Helmke & Levitsky (2004) refer to the role of the legacy of the past in forming the actual institutional make-up of a country. According to the collected data in the Russian context, this legacy is unlikely to be eroded, and on the contrary, may increase in its perceived presence because of the self-perpetuating nature of the Russian government<sup>162</sup>.

On the positive side, greater capacity of the state has increased clarity as to which power structures represent the true authority in the country. In the 1990s it was possible for local administrations and Financial Industrial Groups to determine their own rules of co-operation with major investors in their immediate environment (Brown, Guriev, & Volchkova, 2000). The power was decentralised and therefore the environment was demarcated into separate constituencies with their own institutional peculiarities (e.g. involvement of the Cossack army in the dispute resolution at Knauf-Kubansky Gyps factory). Under Yeltsin, the government claimed control of these power structures, but never really had much influence over what they actually did on their own territory. In perceived terms, the coded

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<sup>162</sup> The Russian political elite survived the change from communism to capitalism. It is a well-known fact that Putin was a KGB agent under the Soviet system and a president and later Prime Minister of supposedly capitalist Russia.

data suggests that it was absolutely not the case in 2006 when the central government very easily extended its administrative resource against rebelling governors and Financial Industrial Groups. As far as foreign investors are concerned, the environment now offers a lot more clarity in terms of exactly who needs to be approached for the authorisation of large commercial deals. But this is where the positive change ends. The gathered data answers the question posed by Pomeranz (2004) about where the property rights would go under Putin. In perceived terms, there is evidence to suggest that the government is readily prepared to change its mind in connection with previously signed agreements about commercial property. In other words, although foreign investors now know who is responsible for regulating the environment and allocating property rights, they also know that there is a real risk of falling out of favour with the government and losing everything. This risk is exacerbated by the apparent unpredictability of the administrative elite and key decision makers within the government. Such an image of the Russian environment will inevitably lead to a new discount on sales of major Russian assets directly proportionate to the perceived risks of this nature. Clearly this fact is recognised by the government itself which is very keen to improve its corporate image by promoting concepts like the rule of law and formal institutions. Unfortunately, the analysed data suggests that in perceived terms these concepts are not maintained with reference to disputes over strategic assets.

Therefore, in the context of pervasive cronyism that stagnates the necessary cultural change, the rule of law will not radiate from the government. This will continue to be the case until the benefits from creating a positive corporate image start to outweigh the gain from crude re-distribution of property (see literature review chapter 2, section 3.1.2). In the context of the ever-rising value of natural resources and struggling global markets this is unlikely to happen.

### 5.3.2 Institutional Change in Russian Corporate Governance: The Role of Private Capital

With reference to conflicts involving private companies and shareholders, collected data suggests that the perception of corporate governance practice in the country has improved. This improvement is determined by a number of positive factors associated with 2006 that were not characteristic of 1998:

- Recognition of private property by immediate stakeholders
- Businesses less bound by social obligations
- More sophisticated corporate culture displayed by shareholders/stakeholders in the instance of a corporate conflict
- Dependence of commercial entities on external financing
- Formal arbitration as an accepted norm
- Less ambiguous environment and more transparent corporate entities.

On the negative side:

- Financial Industrial Groups continue to dominate the corporate environment
- Corporate raids continue to take place
- Secretive culture continues to be a factor.

One of the key improvements within the environment relates to private entities which have become exposed to the control of recognisable corporate governance mechanisms. In particular, creditors and minority shareholders are in a much better bargaining position when it comes to negotiating their end of the deal. In perceived terms this did not happen due to an apparent and significant progress in the development of effective institutions, but because of the dependence of stakeholders on each other (Black & Kraakman, 1996). Large companies need working capital, and finance providers (creditors and shareholders) need to invest their money. The needs of large companies are determined by their owners' wish to protect their own capital (largely from the state) whereas the banks and

investors agree to provide the capital only on certain conditions. Due to the risk of re-nationalisation, private companies need to protect themselves more and more. Banks (particularly foreign) capitalise on this fact by demanding better corporate governance standards. Although the threat of re-nationalisation is generally not good, the vulnerability of current owners forces them to accept ever growing demands of external finance providers. A good demonstration of this point is the disclosure of the identity of RusAl's ultimate beneficiary after it was demanded by the EBRD. Derepaska (100% shareholder of RusAl) needed to accept this condition to protect his own money by receiving a loan from the European bank.

Similar logic applies to foreign minority shareholders who are now in a better position to protect their interests. In Russia, 100% ownership is perceived as a very dangerous position to be in. One of the reasons the Yukos affair was so painful for the Russian government was because of the involvement of foreign minority shareholders who put up a real fight in the international courts suing even top government officials. Had Khodorkovsky (CEO of Yukos) been a 100% owner, the story would not have been published in the newspaper more than once. Private owners in Russia realised this fact and became very keen to invite foreign minority stakeholders. Consequently, corporate behaviour improved because of that keenness (which is stimulated by the risk of losing everything). This provides an insight into how the self-enforcing model of corporate law (Black, 1996) actually evolved in the Russian context.

Additionally, although the capital markets are still perceived as under-developed, transactions involving private companies are naturally gravitating towards appropriate valuations. No longer do severely discounted sales constitute a feature of the perceived environment in the context of private transactions. Hence with regard to private companies, the coded data serves as a confirmation of the findings by Roberts (2004). Moreover, due to the previously mentioned proximity to market valuations major private sales are not typically followed by fierce battles for control. Renegade directors have disappeared from the perceived corporate scene and no longer cause confusion as to who the real owners are. This fact serves as an explanation for the falling degree of violence (often referred to as 'gun battles' in the press) initiated by private parties. Admittedly, if no one

challenges property rights, then there is no need to resort to the extra-judiciary resolution<sup>163</sup>.

Additionally, the inevitable profit-driven agenda of private entities has forced companies to shed their externally imposed social obligations (Fox & Heller, 2000). In perceived terms, the gathered data suggests that the workers collectives (unions) stopped playing as big a role in 2006 as they did in the 1990s. Moreover, there is reduced pressure on major companies to invest in social projects and maintain certain levels of employment. Therefore, in terms of balancing the needs of key stakeholders, there are fewer conflicting demands with which the management typically needs to be concerned (Black & Kraakman, 1996). In this respect, the overall perception is that the government is the only stakeholder whose interests require careful consideration.

In terms of the judiciary, although there is an element of bigger companies' ability to more effectively navigate the court system, the fact that according to the reported material the court rulings are usually complied with suggests greater integrity of the judiciary with reference to private conflicts. In this respect, it is suggested that stronger property rights and the more profit-driven environment have encouraged longer term investments that in turn place greater importance on corporate image, which then forces bigger companies to respect court decisions (even when they have the financial clout to challenge/undermine the judiciary).

In terms of the analysis of the reported data, the most significant drop in reported corporate disputes occurred in relation to private companies. Although corporate raids continue to send shockwaves across investment communities in Russia, in perceived terms, private entities have entered a new era of corporate governance where efficient capital markets, adequate judiciary and cultural integrity are recognisable ingredients in the developing corporate environment in Russia.

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<sup>163</sup> And if the government challenges ownership, then in most cases the perception is that nothing can be done about it.



## 5.4 Original Contribution

1. In terms of the gap in contemporary literature on Russian corporate governance, this study attempts to address the call to generate more enterprise data (Fox & Heller, 2000) and investigate the subject of institutional change in Russian corporate governance. This was achieved by studying company practice from a unique perspective (Iwasaki, 2007). One of the key research outputs of this study is a comprehensive data base of the reported corporate disputes covering the two years of the study. The database (appendices 9a and 9b) can be used by both academics and practitioners by tracing general conclusions back to the detail of the individual company's behaviour. Here, the changes within the reported practice serve as a foundation for inferences about the institutional change in Russia.

2. This study explains the nature of corporate disputes and methods of their resolution based on the analysis of the reported material. It exposes the weaknesses of positivistic categorisations and capitalises on a more flexible coding system. In this context the findings reveal a compelling call for separating state companies from private entities in the analysis of corporate disputes (table 5.1). With reference to state companies, a considerable deterioration has been registered according to the reported practice of such entities. The key negative force here is determined by the acceptance of the culture of selective application of law in favour of state-run companies and at the expense of private shareholders and foreign companies. The exposure of state companies to international capital markets has imposed a number of valid restrictions on their conduct. However, the growing power of these entities poses a question whether even the most developed capital markets will be a strong enough mechanism for aligning the conduct of state-run Russian companies in line with the Western norm. Additionally, the collected data suggests that with reference to private entities there is a noticeable improvement in the way corporate disputes are resolved. This primarily refers to the growing costs of reputational damage *vis-a-vis* foreign investors and market institutions rather than significant improvements in the Russian institutional environment.

3. Although the wide spectrum of generated codes (appendix 6b) is not ideal for quantitative investigations, it illuminates areas not covered by formal frameworks of corporate disputes in Russia (Fox & Heller, 2000; Dyck *et al.*, 2008). This contribution can serve as a basis for expanding the two existing frameworks, as well as inform the development of new ones. Similarly, the nature of enforcement practices (Hendley *et al.*, 1999; Hendley *et al.*, 2000) has been updated and expanded in the context of Russia's continuing transition. Here, future investigations need to focus on administrative levers of the state and litigation (chapter 4, section 4, 4.1.5 and 4.1.7) as the most visible enforcement practices in the country.

Finally, this study utilises the method of template analysis (King, 2004) in its less traditional application. Therefore, the coding experience accumulated in the process constitutes an additional contribution to knowledge. In order to explain the last point in more detail, the researcher's reflections on the method of analysis need to be considered (see chapter 6).

## Chapter Summary

This chapter presented the findings of the study and discussed a number of relevant links to the literature. Table 5.1 summarised the key forces behind the institutional change in Russia and revealed the underlying distinction between the role of state-run and private companies in determining the institutional context in the country. It was concluded that a noticeable deterioration of the institutional context occurred based on the practice of state-run companies and an improvement with regard to the conduct of private entities.

Original contribution of this work has been formulated and identified within the thesis. Firstly, the call for a multi-faceted approach to investigations of corporate governance has been addressed. Secondly, the change in the institutional environment in the country has been analysed from a unique perspective. Thirdly, the categorisation of corporate disputes and methods of their resolution has been developed. Lastly, the main method of analysis has been applied to the reported data in an innovative way.

## Chapter 6: CONCLUSION

### 6.1 Introduction

This chapter briefly reiterates the main findings of the study, provides a detailed revision of the research objectives and also shares reflections on the use of template analysis. The work is concluded by referring to key limitations and further research suggestions.

### 6.2 Institutional Change in Russian Corporate Governance

The study registered institutional change in Russian corporate governance as per the Moscow Times reports. The biggest change occurred in the perceived role of formal institutions and the way the Russian government chooses to employ those while dealing with large businesses. Here, there is little hope for an improved institutional environment because of the culture of key stakeholders within the government who continue to accept the practice of selective application of rules and laws. This conclusion is based on the reported actions that the state exhibited in its drive to re-nationalise some of the assets, particularly in the strategic sectors such as oil and gas. Support for this conclusion lies in the numerous examples of state companies' behaviour revealed by the analysis of the coded material. This practice is imitated by smaller-scale officials who facilitate corporate raids through manufactured allegations against targeted entities. Although the reform to tackle this problem is currently under way, it is likely to produce a limited impact unless the culture of the Russian administrative elite changes accordingly.

With respect to private entities, the reported practice shows a greater degree of reliance on formal institutions in the process of dispute resolution. Although there is a perceived dominance of Financial Industrial Groups, there are also examples of behaviour that accounts for basic corporate governance principles. This shift in attitude of private entrepreneurs is determined by the evolving set of motives that encourage compliance with the law. The growing threat of re-nationalisation has created a pressing need to involve western finance providers since they are seen as more effective guards of property rights. This effectiveness is determined by the fact that the Russian government chooses not to violate the rights of foreign

investors as blatantly as it does in relation to Russian owners. Therefore, private owners in the country are keen to engage in long-term partnerships with western investors. In order to make these partnerships work, the Russian owners feel pressure to display higher standards of corporate governance.

### 6.3 Revisiting Research Objectives

#### 1. Gap in the Literature

The literature on Russian corporate governance is filled with positivistic studies that investigate correlations between certain corporate or institutional characteristics and firm structure and performance (Iwasaki, 2007). Having reviewed most of the studies of this nature, it was possible to see that the existing knowledge about the actual interaction between various institutions and corporate entities is very limited. Fox & Heller (2000) explain this lack of research in terms of the difficulties associated with gaining access to companies in Russia. The literature review (chapter 2) provides an overview of the state of Russian corporate governance and outlines the gap in academic knowledge in the context of this study. Investigations of Russian corporate governance need to be carried out from a wide range of perspectives (Iwasaki, 2007). Hence, the research question was formulated with this in mind. Previous work that helped to formulate and address the research question was considered with maximum detail.

#### 2. Data Collection

The selected method of data collection produced a rich data set for subsequent analysis. The amount of the Moscow Times coverage of corporate disputes was greater than expected. In total over 300 articles were selected covering a wide range of companies, disputes and practices (Chapter 3). The extent of coverage of corporate disputes was varied, but in most cases sufficient for the selected method of coding.

#### 3. Data Analysis

The research question was developed with the available data set and method of analysis in mind. Due to the wide gap in the literature and the fairly unusual

methodology of this study the original contribution of this work was not compromised by the necessary adjustments. Hence the chosen method of data analysis helped the researcher to code a great deal of textual data in a way that was consistent with the research question.

#### 4. Coding

The coding of the textual data was done manually<sup>164</sup>. The selected hierarchy fully covered the data set due to the flexibility of the coding process which is allowed by the method of analysis. Although this fact detracted from the meaningfulness of the numerical overview (chapter 4, section 1), it contributed a great deal to the level of detail captured by the analysis (chapter 4, sections 2, 3 and 4). It is felt that the final codes and their content reflect the nature of corporate disputes covered by the newspaper with a high degree of accuracy.

#### 5. Interviews

Although the interviews were challenging to arrange, it is deemed that the five interviews conducted produced sufficient material to triangulate the extent to which the coded data covered the material reported by the newspaper (Chapter 4, section 5). During the process, invaluable experience of conducting telephone interviews for academic purposes was gained.

#### 6. Findings

The output of data analysis is presented in table 5.1. The table is a detailed summary of factors stimulating and preventing the development of formal corporate governance institutions in the country (Chapter 5). Identification of these forces is necessary in order to understand the dynamics of the institutional change in the country. Although the identified forces were constructed from the reported material and are based on the perception of the environment, it is likely that their applicability can be extended to explain changes in the actual environment.

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<sup>164</sup> This fact allowed the researcher to acquire a great deal of practical experience in this method.

## 6.4 Reflections on the Use of Template Analysis

In methodological terms, this study contributes to the subject of corporate governance by demonstrating how template analysis can be applied to reported material and more specifically corporate disputes. This research exposes various stages of the coding process which accounts for the complexity of the chosen unit of analysis (i.e. corporate disputes). The main benefit of the method is its acceptance of individual interpretations<sup>165</sup>. Here, credibility is maintained by the transparency of the coding process while subjective interpretations highlight the unique intricacies of the data set.

### 1. Unit of Analysis

The data set of this study originates from newspaper articles which were written with the primary purpose of informing the reader. The fact that these articles also address the research question is a by-product. This is different in the case of interview transcripts which are usually created specifically to address certain questions. To remedy this situation it is necessary to select a clear unit of analysis which is easily identifiable. It was discovered that corporate disputes are recognisable in newspaper reports and therefore act as an appropriate filter for selecting relevant articles. This selection process is necessary to ensure that the content of the raw (un-coded) data is consistent with the research question. Therefore, in this context the quality of the data set is contingent upon the level of 'identifiability' of the unit of analysis. Corporate disputes, although recognisable to a reader of articles, cannot be captured inclusively by means of key search words. Hence, appropriate research time needs to be set aside for a careful screening of the content of reported material. This is a very labour intensive task which is best performed manually in order to ensure maximum consistency of the data set and research question.

### 2. Evolution of Codes

Once the data set has been created the task of coding becomes the individual effort of the researcher. It is recognised that the evolution of codes is a creative process that contains an element of subjectivity. This freedom of subjectivity is

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<sup>165</sup> Almost constructionist perspective.

necessary in order to ensure the maximum reach of final codes. However, it is also critical to demonstrate the logic of the decisions made. In other words, the relationship between the codes and the corresponding content must be visible. In this respect, the researcher inevitably takes the risk of failing to expose such a connection. The coding experience of this study leads to the conclusion that in order to minimise such a risk, the relationship between the chosen codes and content must not be too inferential. Template analysis allows additions to and alternations of the employed codes and, therefore, the researcher was able to avoid overly complicated inferences by constantly revising the coding structure.

### 3. Reported Material and Interviews

This research demonstrates how the coded data can be triangulated by means of interviews with the reporters of the newspaper. It is felt that the result is satisfactory because the content of the coded material closely matches the content of conducted interviews. However, this triangulation primarily refers to the coding process and not extended generalisability of the findings. It is understood that the interviewed reporters would most likely refer to disputes they themselves wrote about. Unless there is a serious concern about freedom of speech, the content of the reported material should match the reporters' accounts. This in itself does not contribute anything to the status of the findings. What is an important contribution of triangulation in this context is the fact that no important dispute was omitted from the coding. In this respect, this research invites the triangulation of reported material in order to address concerns about the unit of analysis, the coding process, and the quality of the coded material.

### 4. Usability of the Method

In order to address the call for a multi-faceted approach to investigations of corporate governance in Russia more extensively, a greater use of this technique is completely justified. A great deal more can be learnt about the way institutions evolved in the country by a similar analysis of a different time span and source of media. Additionally, this research focused on the negative reporting associated with corporate disputes. Conversely, the same method can be applied to reported material on good corporate practice in the country. Here, any positive corporate news reported in the newspaper can be a justifiable unit of analysis. Finally, this

method can be used to complement the findings of more generalisable studies by borrowing their units of analysis and applying those to the reported material in a similar way. For example, studies that investigate the effects of ownership (Woodruff, 2004; Melentieva, 2000; Yudaeva *et al.*, 2003) can be exposed to an additional level of scrutiny by analysing reported material in the proposed way.

## 5. Limitations of the Method

It is important to acknowledge that a great deal of diligence and thoughtfulness that is invested in the revision of codes remains largely behind the scenes<sup>166</sup>. Hence, the first limitation of this method is the fact that it relies on the thoroughness of the individual undertaking this method of analysis and his/her integrity as a researcher. The method needs to be treated with caution, particularly when it comes to the status of the findings. It involves an element of subjectivity and cannot function without acknowledging limited generalisability, reliability and validity. In order to address this point, alternative quality checks have to be selected. In connection with this research, credibility and trustworthiness of the findings are achieved by a transparent presentation of the coded data (appendices 9a and 9b as well as chapter 4, sections 2, 3 and 4) and complemented/triangulated by means of the interview material.

Second, because of the flexibility of the coding process, it is difficult to predict the end result of the analysis. The limitation here relates to the applicability of the original data set which very much dictates the extent to which the research question can be addressed. As previously stated, this research relies on the textual data that was not originally created for the purpose of addressing the research question. Hence there is a limitation with regard to the actual applicability of the selected data set. Again as suggested previously, the remedy here is the connection of the research question with the data set through the chosen unit of analysis. If the connection is unclear, the required level of applicability can be questioned.

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<sup>166</sup> It would be an impossible task to take the reader through every stage of the coding process because of the extent of alterations however appendices 6a and 6b present a priori and final codes. Also, chapter 4 sections 2, 3 and 4 present the adopted definitions of the codes.



Third, replicability of the findings cannot be tested. This is because the coding structure evolves constantly and is not ready until the entire data set has been coded. Again, the solution here is the maximum exposure of the coded material which features in chapter 4 (sections 1, 2, 3, 4 and 5).

Finally, graphs and the numerical data presented in chapter 4 are subject to the limitation of the inherent subjectivity of the coding process. Therefore their purpose is to assist the task of presenting the findings and not correlating importance with frequency of reporting. Therefore, the conclusions of this study avoid allocating undue importance to the numerical trends.

## **6.5 Limitations of the Study**

In addition to limitations presented in chapter 3 section 3 and chapter 6, it is important to stress that the findings presented in table 5.1 (chapter 5) primarily register a change in perception of the institutional environment in the country. Although anecdotal evidence (interviews with the Moscow Times reporters) suggests that the newspaper covers corporate conflicts in full, scientifically, this study analysed the expected change in perception, and conclusions about the actual institutional change in the country are inferential.

Second, this study analysed reported material produced by a single newspaper. Although in 1998 it was the only English speaking news provider in the country, in more recent years a number of specialised English speaking media outlets in Russia have been established.

Finally, the time span of the study is limited to two years. Although for a single researcher it is a considerable undertaking, the strength of inferences could have been improved by covering more years.

## **6.6 Further Research**

Further research can address some of the above limitations of this study by expanding the time span and relying on more than a single media outlet.

One of the key lines of enquiry that further research is urged to pursue is extending the comparative dimension to include Russian publications. By comparing coded material produced on the basis of western and Russian media, not only additional knowledge about the subject matter can be extracted, but also important inference about the western bias and the freedom of reporting of corporate events in Russia can be determined. Here, a bilingual researcher will be necessary to ensure systematic coding of articles written in English and Russian.

Second, this work can serve as a foundation for exploring various types of disputes and enforcement practices in more detail. The study produced a number of well defined units of analysis in the form of final codes. For example, the changing nature of private enforcement can be investigated on its own over a longer period of time. The produced content of the code can be used as a basis for developing a framework for further investigations of this type of enforcement practice in Russia and other environments. These more narrowly defined units of analysis are expected to inform more focused investigations with clear policy implications.

Lastly, the subject of institutional change in Russian corporate governance needs to be discussed further as new evidence emerges with time. The same research question can be used in conjunction with a whole spectrum of both qualitative and quantitative methodologies if the complexity of the process is to be fully examined.

## **6.7 Concluding Comment**

The developing nature of corporate governance institutions needs to be under continuous scrutiny by academics. This study provides a useful contribution to understanding the evolutionary aspect of the phenomenon in the context of Russia's continuing transition.

The greatest challenge of this study was determined by the level of complexity of the matter at hand which was accommodated for by the flexibility of the chosen methods of data collection and analysis. This complexity is expected to rise to a new level as Russia becomes more exposed to the global economy. The country's financial markets have been affected a great deal by the current economic

downturn (Adelaja, 2008) despite the existence of a massive stabilisation fund. In political terms, the deficiencies of the system are likely to be temporarily forgotten and replaced by rhetoric against capital markets and in favour of a greater role of the state in corporate affairs in the country. The government will be keen to blame external factors and will likely get support from the public in the short-term. In this context, the institutional reform will lose momentum as both Russian and foreign investors seek to minimise the extent of their financial exposure. Already, the government is resorting to extreme measures of shutting down capital markets at times of extreme volatility in order to protect holdings of certain individuals. Ironically, the current financial crisis represents a substantial opportunity for researchers to learn about the way the crisis is to be handled in the Russian context. The press continuously features reports alleging friendly bail-outs and corporate battles with private shareholders who seek to minimise their losses. Here, the tone set by the government and state companies will determine how the country will overcome the downturn. In any case, the behaviour of key stakeholders will have a significant impact on the future development of the institutional context in the country. However, if Russia is to take its rightful place among key economic powers, the basic premise is still as relevant as ever - the administrative elite in the country must be constrained by uncorrupt formal institutions. In the context of previously unsuccessful attempts the task of building such a system needs to be given overriding priority.

Finally, regardless of the findings of this study that suggest an increased role of the state in corporate affairs in the country, foreign investments will continue to flow into Russia. This fact is largely independent of the success of the government at implementing market reforms and strengthening formal institutions. Here, the bargaining power will continue to be on the Russian side because of the current abundance of natural resources that are simply unavailable elsewhere. This very fact does not render successful reforms as a precondition for receiving much needed foreign investments. Hence, reforms in Russia are unlikely to be prioritised to the same extent as they would have been if the country had to compete for foreign capital and expertise on the same terms as other former Soviet republics. The reforms there are linked to the very survival of the economies and hence have been and are treated much more seriously than in Russia. Consequently, Russia

is suffering from a variation of the Dutch Disease<sup>167</sup> which paradoxically is caused by Russia's inherited wealth. However, the most dangerous downside here is not the crumbling domestic industry (the classic effect of the Dutch Disease), but excessively deconstructive role of the state that pursues its own self-perpetuating style of governance. This style of governance, in immediate terms, blocks governance reforms, but more fundamentally transcends and becomes more embedded in the accepted norms of the society which in turn becomes less equipped to function normally in the context of the free market setting.

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<sup>167</sup> The term Dutch Disease refers to the adverse effects on manufacturing that natural resource discoveries have essentially through the subsequent appreciation of real exchange rate. The term originates from the 1960s Holland when the local economy suffered from gas discoveries and subsequent appreciation of the Dutch guilder (Corden, 1984).

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## Appendix 1 a: Background Information about the Moscow Times

**THE MOSCOW TIMES** Part of Independent Media-Sanoma Magazines Publishing House.

### Hard Copy

Published Since	1992
Format	A3
Volume	16-32
Language	English
Frequency	Monday through Friday
Circulation, number of copies	35,000
Readership over six months	357,400
Readership per single issue	26,600
Current Editor:	Andrew McChesney
Business Editor:	Tim Wall

Distribution system — distributed for free in over 500 of Moscow's most prestigious locations such as business centres, international airlines, embassies, hotels, medical centres, restaurants, supermarkets and sport clubs.

### On Line: [www.themoscowtimes.com](http://www.themoscowtimes.com)

Readership:	20,000 visitors per day
Audience:	25% Russian, 75% foreign

The website is particularly popular with representatives of the following industries: -  
Finance and Insurance Banking

- Academic Research
- IT and Telecommunication
- Education
- Government and Public Services

28.7% of readers are top managers of Russian and Western companies in Russia and abroad.

Archive: 139,000 articles covering over a decade of news events in Russia and around the world

Content: General News, Business, Opinion, World, Real Estate, Job Opportunities, Mini-guide, Sports, Arts & Ideas

*Source: NRS Gallup Media, NRS Moscow (September 2007 – February 2008)*

### **Appendix 1 b:** *Opinion of the Moscow Times reporters about the paper's independence and influence*

*'...the readership of the newspaper is not big enough to be on the Kremlin's radar and therefore its reporting is free from political pressure, which most Russian language newspapers have to deal with'.*

*Certainly, it gave an accurate portrayal of many of the problems of corporate governance because they tend to focus on those kind of things, right? Because they were news.*

*The Moscow Times coverage was very important for foreign perception; first of all the foreigners in Moscow read it and the people who were interested in Russia read it and it had an influence on all the foreign correspondence in Moscow so what the Moscow Times wrote influenced what the New York Times wrote. I know plenty of cases where the journalists – the correspondents working for the foreign papers would pick up on stories that were first reported in the Moscow Times including the Economist.*



## Appendix 2: Framework of Russian Corporate Governance Pathologies

<b>I. Non -Maximization of Residuals<sup>168</sup></b>	
<p><u>Pathology 1:</u> Unreformable value-destroying firms fail to close</p>	<p>Arises when an unreformable value-destroying firm can dissipate cash reserves or salvageable assets. Corporate governance is not the key issue when a firm has no reserves or salvageable assets, or when subsidies or unsuitable credits are present.</p>
<p><u>Pathology 2:</u> Viable firms fail to use existing capacity efficiently</p>	<p>Arises when continued firm operation, if undertaken as efficiently as possible and without new investment, would be a positive net present value (NPV) decision; but costs are not minimized, the best price is not obtained for given output, or a non profit-maximizing output level is chosen.</p>
<p><u>Pathology 3:</u> Firms misinvest internally generated cash flows</p>	<p>Arises when a firm uses internally generated cash flow to invest in new negative NPV projects instead of paying out this cash flow to shareholders who could invest the funds better elsewhere in the economy.</p>
<p><u>Pathology 4:</u> Firms fail to implement positive NPV projects</p>	<p>Arises when a firm identifies but then fails to act on positive NPV projects. Managers tend to be averse to risk because they cannot diversify away from unsystematic risk of a firm's project. If others do not pick up the opportunity, the firm's failure also reduces social welfare.</p>
<p><u>Pathology 5:</u></p>	<p>Arises when a firm's managers fail to identify positive NPV projects that the firm is particularly well</p>

<sup>168</sup> This framework of corporate governance pathologies served as a basis for the development of some of the themes and codes. However, it is critically important to point out that the final codes are defined by the actual content and not their a priori meaning.

Firms fail to identify positive NPV projects	positioned to find. The possibility of venture financing and spin-offs can reduce the prevalence and social costs of this pathology.
<b>II. Non Pro Rata Distributions</b>	
<u>Pathology 6:</u> Firms fail to prevent diversion of claims	Arises when some residual owners of a firm manipulate corporate, bankruptcy, and other laws to shift ownership away from other residual owners – often by diluting shares held by outside minority shareholders.
<u>Pathology 7:</u> Firms fail to prevent diversion of assets	Arises when some residual owners privately appropriate assets and opportunities belonging to the firm, but leave the firm's formal ownership structure intact.

Source: Fox & Heller, (2000)

### Appendix 3: Example of an article containing a corporate dispute

Tuesday, October 27, 1998.

#### **Moscow Court Seizes 330 Rossiisky Kredit Vehicles**

By Boris Aliabyev

Bailiffs have seized 330 cars and armoured vehicles owned by Bank Rossiisky Kredit, acting on a court ruling in favour of a disgruntled bank client.

Moscow's Golovinsky District Court ordered the seizure of the property last week to support a claim by a computer firm called Trekhmernaya Pamyat, or Three-Dimensional Memory, based in Oryol, a city about 400 kilometres southwest of Moscow, bailiff Maria Khrenova said Monday. Moscow's traffic police assisted the bailiffs in seizing the cars, she added.

Trekhmernaya Pamyat won a ruling against Rossiisky Kredit in Moscow City Arbitration Court in September, said the firm's lawyer Sergei Yerokhov. The court ruled that Rossiisky Kredit had wrongfully refused to transfer 32 million rubles (\$1.9 million at Tuesday's official rate), meant for wages and taxes, out of the computer company's account. According to Yerokhov, the seized cars are worth \$2 million.

The Golovinsky Court has jurisdiction over the area in Moscow where Rossiisky Kredit is registered. It has recently issued over 40 rulings against the bank, which are now being enforced, a court official said.

Rossiisky Kredit was one of Russia's top banks before the Aug. 17 ruble devaluation and debt default. Some of its depositors and clients have since filed a suit against the bank to recover their money. Vladimir Zimonenko, a lawyer who works for several Rossiisky Kredit depositors, told Reuters last week that he had won one of these cases, in which his client demanded \$8,000 from the bank.

Numerous suits are pending against other Russian banking giants also, for example, more than 5,000 of them have been filed against SBS-Agro bank in another area of Moscow.

But the Trekhmernaya Pamyat case dates to events that took place before Aug. 17. The bank says it had refused to transfer Trekhmernaya Pamyat's money because the firm's account had been frozen by tax authorities in Oryol last summer. Rossiisky Kredit spokeswoman Tatyana Izmailova said the bank would appeal the arbitration court ruling.

The computer company's lawyers said, however, that the tax authorities had no problem with their client and the bank was just trying to hang on to the money.

#### **Appendix 4: Interview Guide**

##### **Introduction:**

The questions below address the corporate governance environment in Russia. They seek to:

1. Cover corporate disputes and methods of their resolution pertaining to and representative of 1998 and 2006.
2. Invite comments on the rule of law/ (or lack of it) as determined by the dominance of both formal and informal institutions.
3. Address the role of The Moscow Times and press in covering corporate disputes.

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**Interviewees:** Three reporters working for the Moscow Times in 1998<sup>169</sup>

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##### **Questions in relation to late 1990s Russia:**

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<sup>169</sup> All published material produced by the reporters was reviewed before the interviews in order to help participants recall particularly memorable disputes and be in a better position to probe the questions further.

### **1. Disputes:**

Are there any particular corporate disputes that come to mind?

Possible answers:

- 1. Managerial (non- maximization of residuals)**
  1. *Bankruptcy*
  2. *Ownership*
  3. *Misinvestment*
  4. *Misimplementation*
  5. *Taxes*
  6. *Control*
- 2. Distributions (unfair distribution of residuals)**
  7. *Diversion of Assets*
  8. *Diversion of Claims*
- 3. Other**

*Probe<sup>170</sup>: What was the problem? Who were the key parties involved in the disputes?*

### **2. Enforcement:**

What were the most effective ways of resolving such corporate disputes?

Possible answers:

1. *Litigation (courts)*
2. *Administrative levers of the state (officials exercising influence)*
3. *Private enforcement (private enforcement agencies, security firms)*
4. *Third-party enforcement (influential organisations)*
5. *Self- enforcement (own capabilities)*
6. *Shadow of enforcement (threat of resorting to a stronger enforcement mechanism)*
7. *Relationship-based enforcement (negotiations, mutual agreement, compromise)*
- 8. Other**

*Probe: Who was involved in the arbitration process? Which party/stakeholder group prevailed and why? How fair was the arbitration process?*

### **3. Institutional Environment and the Rule of Law**

To what extent were the identified methods of dispute resolution determined by the existing institutional environment?

*Probe: What were the most dominant institutions/mediators at the time? Which institutions were stronger at the time? How would you comment on the rule of law at the time?*

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<sup>170</sup> Suggested by King, (2004).

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**Interviewees:** Two reporters working for the Moscow Times in 2006

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The same set of questions is then asked in relation to modern day (2006) Russia.

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**Interviewees:** All five reporters working for the Moscow Times

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Additionally, two questions specifically about the Moscow Times were asked:

**4. The role of the Moscow Times**

4. a How accurate was/is the Moscow Times coverage of corporate disputes?

*Probe: If accurate/inaccurate – why? Any political, economic or other pressures?  
Any sources of possible bias?*

4. b How much of foreign investor perception was/is determined by the Moscow Times coverage of the environment?

*Probe: How does the newspaper coverage of disputes influence actual corporate practice?*

**Appendix 5: Informed consent form for research participants**

<b>Title of Study</b>	<b>Institutional Change in Russian Corporate Governance: An Analysis of Corporate Disputes</b>
Person(s) conducting the research	Roman Stepanov
Programme of study	PhD
Address of the researcher for correspondence	Newcastle Business School City Campus East Newcastle Upon Tyne NE1 8ST
Telephone	+44(0)191 2347660 or +44(0)7949120617
E-mail	<a href="mailto:roman.stepanov@unn.ac.uk">roman.stepanov@unn.ac.uk</a>
Description of the broad nature of the research	Arguably, the two major determinants of corporate governance in the Russian context are shareholder rights and law enforcement practices. Over the years, practical solutions employed in relation to these determinants deviated from the Western model by far more than any other aspect of corporate governance. The first stage of the study proposes to address the evolutionary change within these determinants by examining corporate disputes and enforcement strategies prevailing in 1998 and 2006 in Russia.

<p>Description of the involvement expected of participants including the broad nature of questions to be answered or events to be observed or activities to be undertaken, and the expected time commitment</p>	<ul style="list-style-type: none"> <li>• Participants will be expected to share their knowledge/experience of typical corporate disputes pertaining to 1998 and 2006 in Russia.</li> <li>• Participants will be asked about enforcement strategies used in relation to the disputes identified.</li> <li>• Participants will be asked to comment on the institution change in Russia over the period in question</li> <li>• Interviews will last approximately half an hour and participants will be asked whether they consent to the interview being recorded. They do not have to do so.</li>   <li>• Participants will later be offered the chance to read a transcript of the interview and amend it if they wish to.</li> </ul> <p><b>Participation is entirely voluntary</b> and participants can refuse to answer certain questions or end the interview at any time.</p>
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Information obtained in this study, including this consent form, will be kept **strictly confidential** (i.e. will not be passed to others) and **anonymous** (i.e. individuals and organisations will not be identified *unless this is expressly excluded in the details given above*).

Data obtained through this research may be reproduced and published in a variety of forms and for a variety of audiences related to the broad nature of the research detailed above. It will not be used for purposes other than those outlined above without your permission.

Participation is entirely voluntary and participants may withdraw at any time.

By signing this consent form, you are indicating that you fully understand the above information and agree to participate in this study on the basis of the above information.

*Participant's signature*

*Date:*

***Student's signature Roman Stepanov***

***Date:***

Please keep one copy of this form for your own records



## Appendix 6 a: *A Priori Themes*

### Corporate Disputes

- Non-Maximization of Residuals (5 Pathologies)
- Non Pro Rata Distributions (2 Pathologies)

*(Fox & Heller, 2000)*

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### Corporate Disputes: Parallel Themes

- Appraisal of Assets
- Inaccurate/Incomplete Information
- Voting
- General Meetings
- Share Dilution
- Insider Dealing
- Transfer Pricing
- Asset Stripping
- Transactions with Self Interest

*(Federal Law 'On Joint Stock Companies' dated 1995, last amended 2006)*

- **Other**

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### Enforcement Strategies

- Litigation (courts)
- Administrative levers of the state (officials exercising influence)
- Private enforcement (private enforcement agencies, security firms)
- Third-party enforcement (influential organisations)
- Self-enforcement (own capabilities)
- Shadow of enforcement (threat of resorting to a stronger enforcement mechanism)
- Relationship- based enforcement (negotiations, mutual agreement, compromise)

*(Hendley et al., 1999)*

- **Other**

## Appendix 6 b: Final Themes

### Corporate Disputes

- Bankruptcy 1.1.1
- Ownership/Structure 1.1.2
- Misinvestment 1.1.3
- Misimplementation 1.1.4
- Tax 1.1.5
- Control 1.1.6
- Diversion of Assets 1.2.1
- Diversion of Claims 1.2.2

*(Based on Fox & Heller, 2000)*

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### Corporate Disputes: Parallel Themes

- State Interference D1
  - Inadequate Information D2
  - General Meetings D3
  - Unclear Rules D4
  - Transactions with Self-Interest/  
Transfer Pricing/Insider Dealing/ D5
- Asset Stripping/Appraisal of Assets
- /Share Dilution

*(Based on the Federal Law 'On Joint Stock Companies')*

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### Enforcement Strategies

- Relationship-Based ES6

- Self-Enforcement ES7
- Third-Party Enforcement ES8
- Private Enforcement ES9
- Administrative Levers of the State ES10
- Shadow of Enforcement ES11
- Litigation ES12

*(Based on Hendley et al., 1999)*

### Appendix 7 a: Companies and Respective Industries, 1998

Industry	Ref.	Company	Notes
Transport	1.	Aeroflot	Airline
Telecommunications	3.	MGTS	Mobile phone network provider
	4.	VimpelCom	Mobile phone network provider
Automotive	6.	AvtoVaz	Car manufacturer (Lada)
	7.	Gaz	Car manufacturer
	8.	KamAZ	Heavy truck manufacturer
	9.	KIA Motors	Car manufacturer
Oil & Gas	10.	Rosneft	State oil company

	11.	Gazprom	State gas company
	12.	Yukos	Private oil company
	18.	Transneft	State oil pipeline company
	19.	Surgutneftegaz	Private oil company
	20.	Tatneft	Private oil company
	21.	Sibneft	Private oil company
	22.	Sidanko	Private oil company
	23.	Tyumen Oil Co	Private oil company
Energy	24.	Krasnoyarsk Hydro Plant	Hydro plant
	25.	UES	Electricity provider
	26.	Mosenergo	Moscow electricity provider
Manufacturing of Generators	27.	Electrosila	Manufacturer of power generators
Metallurgy	28.	Norilsk Nickel	Nickel miner
	29.	Novolipetsk	Steel mill
	33.	Magnitogorsk	Steel mill
	34.	Libedinsky Ore Mining Plant	Ore mining plant
	35.	Achinsk Alumina Combine	Alumina combine
Construction Materials	36.	Knauf	Construction materials
Paper Mill	38.	AssiDoman	Paper mill
	39.	Vyborg Paper	
Banking	40.	SBS - Agro	Bank
	41.	MFK Renaissance	Investment bank
	42.	Inkombank	Private bank
	43.	MOST Bank	Private bank
	44.	Pioneer Group	Foreign Bank
	45.	EBRD	European bank

	46.	Tokobank	Private bank
	47.	Rossiisky Kredit	Private bank
Media	49.	Kosmos	Cable TV company
	50.	Channel Five	St. Petersburg TV channel
	51.	ORT	Main Russian TV channel
Food	52.	Subway	Fast food
Porcelain	53.	Lomonosov Porcelain Factory	Porcelain factory
Coal Mining	54.	Kuznetsky Mine	Coal Mining
Real Estate	55.	MCCI	State-owned real estate company
Auto Parts	56.	Standart - NMT	Auto parts distributor
Logistics	57.	Post Office	Post office

#### Appendix 7 b: Companies and Respective Industries, 2006

Industry	Ref.	Company	Notes
Transport	1.	Aeroflot	State-owned airline
Telecommunications	2.	Svyazinvest	Telephone land line company
	4.	VimpelCom	Mobile phone operator
	5.	Megafon	Mobile phone operator
Automotive	6.	AvtoVaz	Car manufacturer (Lada)
Oil & Gas	10.	Rosneft	State oil company
	11.	Gazprom	State gas company
	12.	Yukos	Former private oil company
	13.	Shell	Foreign oil company
	14.	Total	Foreign oil company
	15.	ExxonMobil	Foreign oil company

	16.	TNK-BP	Foreign oil company
	17.	LUKoil	Private oil company
	18.	Transneft	State-owned oil pipeline
Metallurgy	29.	Novolipetsk	Steel mill
	30.	Severstal	Steel mill
	31.	Evrz	Steel mill
	32.	RusAl	Aluminium producer
Construction Materials	37.	Eurocement	Cement
Retailer	48.	IKEA	Furniture and renting of retail space

**Appendix 8 a: Template of the Coding Profile – Management**

**First order**

1.1 Management	1.2 Diversion
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**Second order**

1.1.1 Bankruptcy	1.1.2 Ownership	1.1.3 Misinvestment	1.1.4 Misimplementation	1.1.5 Taxes	1.1.6 Control
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**Third order**

Disputes/Enforcement

<b>D1</b> State Interference	<b>1.1.1.1</b>	<b>1.1.2.1</b>	<b>1.1.3.1</b>	<b>1.1.4.1</b>	<b>1.1.5.1</b>	<b>1.1.6.1</b>
<b>D2</b> Inadequate Information	<b>1.1.1.2</b>	<b>1.1.2.2</b>	<b>1.1.3.2</b>	<b>1.1.4.2</b>	<b>1.1.5.2</b>	<b>1.1.6.2</b>
<b>D3</b> General Meeting	<b>1.1.1.3</b>	<b>1.1.2.3</b>	<b>1.1.3.3</b>	<b>1.1.4.3</b>	<b>1.1.5.3</b>	<b>1.1.6.3</b>
<b>D4</b> Unclear Rules	<b>1.1.1.4</b>	<b>1.1.2.4</b>	<b>1.1.3.4</b>	<b>1.1.4.4</b>	<b>1.1.5.4</b>	<b>1.1.6.4</b>
<b>D5</b> Transactions with Self-Interest	<b>1.1.1.5</b>	<b>1.1.2.5</b>	<b>1.1.3.5</b>	<b>1.1.4.5</b>	<b>1.1.5.5</b>	<b>1.1.6.5</b>
ES6 Relationship-Based	1.1.1.6	1.1.2.6	1.1.3.6	1.1.4.6	1.1.5.6	1.1.6.6
ES7 Self-Enforcement	1.1.1.7	1.1.2.7	1.1.3.7	1.1.4.7	1.1.5.7	1.1.6.7
ES8 Third-Party Enforcement	1.1.1.8	1.1.2.8	1.1.3.8	1.1.4.8	1.1.5.8	1.1.6.8

ES9 Private Enforcement	1.1.1.9	1.1.2.9	1.1.3.9	1.1.4.9	1.1.5.9	1.1.6.9
ES10 Administrative Levers	1.1.1.10	1.1.2.10	1.1.3.10	1.1.4.10	1.1.5.10	1.1.6.10
ES11 Shadow of Enforcement	1.1.1.11	1.1.2.11	1.1.3.11	1.1.4.11	1.1.5.11	1.1.6.11
ES12 Litigation	1.1.1.12	1.1.2.12	1.1.3.12	1.1.4.12	1.1.5.12	1.1.6.12



**Appendix 8 b: Template of the Coding Profile – Diversion**

**Second order**

1.2.1	1.2.2
Diversion of Assets	Diversion of Claims

**Third order**

Disputes/Enforcement

<b>D1</b> State Interference	<b>1.2.1.1</b>	<b>1.2.2.1</b>
<b>D2</b> Inadequate Information	<b>1.2.1.2</b>	<b>1.2.2.2</b>
<b>D3</b> General Meeting	<b>1.2.1.3</b>	<b>1.2.2.3</b>
<b>D4</b> Unclear Rules	<b>1.2.1.4</b>	<b>1.2.2.4</b>
<b>D5</b> Transactions with Self-Interest	<b>1.2.1.5</b>	<b>1.2.2.5</b>
ES6 Relationship-Based	1.2.1.6	1.2.2.6
ES7 Self-Enforcement	1.2.1.7	1.2.2.7
ES8 Third-Party Enforcement	1.2.1.8	1.2.2.8
ES9 Private Enforcement	1.2.1.9	1.2.2.9
ES10 Administrative Levers	1.2.1.10	1.2.2.10
ES11 Shadow of Enforcement	1.2.1.11	1.2.2.11
ES12 Litigation	1.2.1.12	1.2.2.12



**Appendix 9 a: Templates of Corporate Disputes, 1998**

**1. Aeroflot: Rao, (1998a) 1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Disputed transactions.
1.2.2 Second Order	Diversion of Claims	Travel agents were told to pay for tickets in advance using the services of a bank connected to majority shareholder.
1.2.2.5 Third Order	Transactions with Self-Interest	Berezovsky personally benefited from the deal.
1.2.2.10 Third Order	Administrative Levers of the State	Berezovsky was under investigation for siphoning the company's assets, but ultimately, the charges were dropped as Yeltsin intervened.
1.2.2.11 Third Order	Shadow of Enforcement	Travel agents considered legal action.

**3. MGTS: Baker-Said, (1998i); Baker-Said, (1998k); Peach, (1998a); Whalen, (1998s) 4 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Disputed transactions.
1.2.2 Second Order	Diversion of Claims	Issue of new shares.
1.2.2.2 Third Order	Inadequate Information	The privatization tender agreement was not disclosed in the company's reports and investment prospectus.
1.2.2.4 Third Order	Unclear Rules	There was a conflict between the Joint Stock Company Law and 1995 investor tender agreement (privatization).

1.2.2.5 Third Order	Transactions with Self-Interest	<p>The majority stake in MGTS was transferred from the Moscow Committee of Science and Technology, a city owned organisation, to AO Sistema, a secretive outfit that had links to Yury Luzhkov (the mayor of Moscow).</p> <p>MGTS shareholders voted to allow the company's board of directors to raise authorized capital by 50 percent in preparation for a share issue. The Moscow city government was expected to scoop up the new shares at a highly discounted price under the terms of the 1995 privatization of MGTS.</p>
1.2.2.6 Third Order	Relationship-Based	Svyazinvest and the Moscow City Government were expected to reach a compromise further to a murky share issue in Moscow City Telecom Co. (MGTS).
1.2.2.10 Third Order	Administrative Levers of the State	A presidential decree 1210 ruled in Luzhkov's favour. It was speculated that MGTS' available cash would be spent on the presidency campaign for Yury Luzhkov.

#### 4. VimpelCom: Kenyon, (1998d); Rao, (1998g) 2 articles

Code	Theme	Notes
1.1 First Order	Management	Protection of the business
1.1.6 Second Order	Control	A local criminal community was trying to take control of the company.
1.1.6.5 Third Order	Transactions with Self-Interest	First Deputy Prime Minister Yury Maslyukov was accused of helping VimpelCom illegally obtain a license to operate GSM900 standard. If Yavlinsky's allegations were true, there must have been some kind of behind the scenes agreement involving money.
1.1.6.9 Third Order	Private Enforcement	There were death threats and physical assaults on the company's employees. The attacks were thought to have come from a local criminal community which was trying to take control of the company.

1.1.6.10 Third Order	Administrative Levers of the State	There were allegations that VimpelCom obtained the license to operate the GSM900 standard illegally by relying on the help from First Deputy Prime minister Yury Maslyukov (a fierce defence industry lobbyist).
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#### 6. AvtoVAZ: Whitehouse, (1998a) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Disputed transactions
1.2.2 Second Order	Diversion of Claims	Distributors charged unusually high margins on retail sales.
1.2.2.5 Third Order	Transactions with Self-Interest	The company had a highly criminalised dealership network which was taking unusually high margins on retail sales.
1.2.2.9 Third Order	Private Enforcement	When Kadannikov (director of AvtoVaz) announced a campaign to rework the relationship with the dealers, the company's deputy commercial director was murdered and the director of the spare parts centre was severely beaten.

#### 7. Gaz: Boyle, (1998) 1 article

Code	Theme	Notes
1.1 First Order	Management	Efforts to minimize expenditure.
1.1.5 Second Order	Taxes	Promised tax-breaks did not materialise.
1.1.5.1 Third Order	State Interference	The government granted the joint venture a series of tax breaks which it was forced to withdraw subsequently.

1.1.5.4 Third Order	Unclear Rules	Yeltsin signed a vaguely worded decree granting the auto industry a series of tax breaks and financial incentives. But the tax-breaks fell foul of existing legislation and the International Monetary Fund's requirements.
1.1.5.8 Third Order	Third-Party Enforcement	Russia's dependence on the IMF funding forced authorities to scale back on the tax-breaks promised by the presidential decree.

### 8. KamAZ: Peach, (1998j); Rao, (1998c) 2 articles

Code	Theme	Notes
1.2 First Order	Diversion	Dept restructuring
1.2.2 Second Order	Diversion of Claims	Issue of convertible bonds on terms unfavourable for small shareholders and some creditors.
1.2.2.5 Third Order	Transactions with Self-Interest	The debt restructuring plan diluted shares of some small shareholders. Creditors were offered shares based on book value (further to a recent re-valuation of assets) of the company and not the market value (the truck maker's stock was highly illiquid at the time). In effect, \$3 of debt were exchanged for a bond that could be subsequently converted into 1 KamAZ share which was worth a mere \$0.10.
1.2.2.6 Third Order	Relationship-Based	Further to the proposed plans of debt restructuring, KKR partner Michael Tokarz said in a statement that all the sides had agreed to discuss rebuilding KamAZ "in a way that involves and satisfies everyone." KKR has agreed to a dilution of its stake.

### 9. KIA: (Parallel Coding) Rao, (1998d) 1 article

Code	Theme	Notes
1.1	Management	Competition
1.2	Diversion	

First Order		
1.1.5 1.2.2 Second Order	Taxes Diversion of Claims	Disputed seizure of assets further to tax allegations.
1.1.5.8 1.2.2.8 Third Order	Third-Party Enforcement	Allegedly, the tax authorities were in cahoots with the local used cars importers.
1.1.5.10 1.2.2.10 Third Order	Administrative Levers of the State	The tax police targeted (specifically) the KIA venture which cut into the profits of used cars importers.

## 10. Rosneft (3 separate disputes)

**10.1:** 'Criminal Investigation Begins Into Purneftegaz Sell-Off Deal', (1998); Peach, (1998e); Peach, (1998g); Peach, (1998k); Peach, (1998n); 'Rosneft Gets New Chief', (1998); 'Rosneft Unit Stake Sold for Only \$10M', (1998); 'Yeltsin on Purneftegaz', (1998) **8 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Dealing with creditors
1.2.1 Second Order	Diversion of Assets	Dispute over diversion of assets from the state by the company's creditors.
1.2.1.1 Third Order	State Interference	The government ordered to reverse the transaction which deprived state-controlled Rosneft of a stake in its subsidiary Purneftegaz.
1.2.1.5 Third Order	Transactions with Self-Interest	The 38 percent stake in Purneftegaz was seized by the creditors and sold for just \$10 million. Rosneft claimed the stake was worth \$400 to \$500 million.

1.2.1.2 Third Order	Inadequate Information	The true owner of the four obscure companies that had bought the shares was unknown. The Moscow Times traced possible links to industrial giant LUKoil and Kremlin insider Pavel Borodin, while the effective buyer of the stake was directly related to the Moscow Patriarchate.
1.2.1.10 Third Order	Administrative Levers of the State	President Boris Yeltsin intervened to stop the controversial giveaway of the shares in the government-controlled oil company and to punish those responsible for the transaction. Analysts suggested that the court case could go either way, although with the president and prime minister involved, a decision favouring Rosneft and therefore the government was expected.
1.2.1.12 Third Order	Litigation	Analysts suggested that the court case could go either way, although with the president and prime minister involved, a decision favouring Rosneft and therefore the government was expected <sup>171</sup> . Furthermore, a Western bank purchased the stake and in turn sold it back to a Russian entity. It was necessary to bring a Western financial institution into the deal since Russian law enforcement agencies "wouldn't crack down on a Western bank as they would on a Russian bank in the event of a scandal."

## 10.2: Peach, (1998l); Whalen, (1998j) 2 articles

Code	Theme	Notes
1.2 First Order	Diversion	Disputed transactions.
1.2.2 Second Order	Diversion of Claims	Diversion of claims through transfer pricing and write – offs of bad debts.

<sup>171</sup> The reason for coding the same bit of text (theme) a number of times is because the general content is then captured more fully. Template analysis allows this flexibility, at the expense of the relationship between salience and importance (King, 2004).



1.2.2.5 Third Order	Transactions with Self-Interest	Transfer pricing of crude oil and insider dealing in the form of boosting operational expenses by means of write – offs of bad debts belonging to management controlled companies.
1.2.2.6 Third Order	Relationship-Based	It is difficult to imagine a transfer-pricing scheme between two separate companies without a close personal connection between the benefiting parties. In this case, it was the managers/beneficiaries of Purneftegaz and Sibneft.

### 10.3: Peach, (1998) 1 article

Code	Theme	Notes
1.1 First Order	Management	Authority of the board of directors.
1.1.6 Second Order	Control	Dispute over the level of control that the directors had in relation to large transactions.
1.1.6.3 Third Order	General Meeting	At an annual shareholder meeting Rosneft pushed through an amendment to the company's charter giving the board of directors of Purneftegaz authority to conduct transactions with up to 50 percent of the company's assets. Charter amendments require a 75 percent vote, but Rosneft was able to eke out a favourable verdict due to the fact that only 75 percent of Purneftegaz's votes were present at the meeting, thereby giving its 51 percent stake a 68 percent weighing.
1.1.6.7 Third Order	Self-Enforcement	... finding the other 7 percent was a matter of bargaining and subtle stealth. It was suspected that the whole voting procedure was designed/planned by senior management of Rosneft.

## 11. Gazprom (7 separate disputes)

### 11.1: Whitehouse, (1998d) 1 article

Code	Theme	Notes
1.1 First Order	Management	Trading of stock
1.1.2 Second Order	Ownership	Gazprom managers barred foreigners from buying domestic Gazprom stock, and implemented something traders call "the right to the first night," under which the company's registrar refuses to accept trades unless the shares have first been offered to Gazprom.
1.1.2.1 Third Order	State Interference	Yeltsin signed a decree limiting foreign ownership in Gazprom to 9 percent and legalizing the company's ban on direct purchases of domestic shares by foreigners and foreign-owned companies.
1.1.2.4 Third Order	Unclear Rules	Creative foreign investors found ways around the rules. Regent Fund Management Limited set up a Cayman Islands-based entity called Regent GAZ, which announced plans to buy \$200 million worth of domestic Gazprom shares and sell derivatives to foreign investors.
1.1.2.7 Third Order	Self-Enforcement	Gazprom director Rem Vyakhirev publicly denounced the scheme, and subsequently Regent GAZ closed shop.

**11.2: 'Duma Gazprom Plea', (1998); Aliabyev, (1998); Budrys, (1998) 3 articles**

Code	Theme	Notes
1.1 First Order	Management	Management of subsidiaries
1.1.5 Second Order	Taxes	Russian tax police seized the assets of two Gazprom subsidiaries as part of a campaign by newly appointed tax chief Boris Fyodorov to increase revenue collection.
1.1.5.1 Third Order	State Interference	The State Duma, or lower house of parliament, moved against the seizure by adopting a resolution which portrayed the action as a threat to national security.

1.1.5.10 Third Order	Administrative Levers of the State	The government and Gazprom were expected to reach a compromise in which Gazprom would agree to shoulder some of its subsidiaries' debts and the government would delay enforcing the bankruptcies.
1.1.5.11 Third Order	Shadow of Enforcement	Gazprom responded by saying that the seizure assets would cause far-reaching economic consequences.

### 11. 3: Whalen, (1998aa) 1 article

Code	Theme	Notes
1.1 First Order	Management	Reforming gas industry
1.1.2 Second Order	Ownership	Demands to increase transparency by reforming the ownership structure of Gazprom's pipeline network.
1.1.2.1 Third Order	State Interference	The government had to restructure the gas market if it was to receive the loan from the World Bank.
1.1.2.8 Third Order	Third-Party Enforcement	The World Bank sought to enforce the decision by stating that the \$1.5 billion loan to Russia was on condition that the government would reform the gas company.

### 11. 4: 'Gazprom Challenged', (1998) 1 article

Code	Theme	Notes
1.1 First Order	Management	Trust agreement.
1.1.2 Second Order	Ownership	Russia's independent Federal Audit Chamber said that it was seeking to cancel an agreement under which the head of gas monopoly Gazprom also managed the 35 percent stake owned by the state. The trust agreement between the government and Gazprom chief executive Rem Vyakhirev was signed in December 1997. The new agreement was intended to limit Vyakhirev's power by denying Gazprom the right to buy up to 30 percent of the company's shares at face value, an option available under the previous trust arrangement.
1.1.2.1 Third Order	State Interference	Head of Gazprom (Vyakhirev) fell out of favour with the government which used the Audit Chamber to limit his powers by cancelling the trust agreement. The original trust agreement delegated management of the state's 35 percent stake to the head of Gazprom i.e. Vyakhirev.
1.1.2.12 Third Order	Litigation	The chamber proposed to the Prosecutor General's Office to start court proceedings aimed at declaring the original agreement illegal and therefore null and void.

#### 11.5: Peach, (1998h) 1 article

Code	Theme	Notes
1.1 First Order	Management	Purchasing decisions
1.1.3 Second Order	Misinvestment	Decisions to purchase Inkombank and a media outlet were more likely to be motivated out of pre-election oligarchic manoeuvring rather than prudent business acumen.

1.1.3.1 Third Order	State Interference	Gazprom purchased a 25 percent stake in Inkombank, and grew its media portfolio; these actions were motivated by pre-election oligarchic maneuvering rather than prudent business acumen. It has been suggested that Gazprom was worried about its oligarchic friends first, the government second, employees third, and then maybe its shareholders.
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#### 11. 6: Peach, (1998b) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Privatisation auction.
1.2.1 Second Order	Diversion of Assets	A large equity stake in a strategic natural-gas refining company was sold off to an unknown European company for roughly \$20 million, a price significantly below the company's value.
1.2.1.5 Third Order	Transactions with Self-Interest	A natural gas refining company was sold for very cheap in a privatisation tender to an unknown European company. The premium of only \$11,420 was paid on the extremely low starting price of \$20 million.
1.2.1.2 Third Order	Inadequate Information	No information about the buyer was made available by the privatization officials, although fingers in the industry immediately and instinctively pointed to Gazprom, which possesses other major gas refineries in Russia and was likely interested in obtaining more.
1.2.1.10 Third Order	Administrative Levers of the State	Such a sale was authorised and facilitated by the privatisation officials close both to the company and government.

### 11.7: Arvedlund, (1998) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Barter
1.2.2 Second Order	Diversion of Claims	The problem of theft through barter extended to Russia's biggest companies, including Gazprom.
1.2.2.5 Third Order	Transactions with Self-Interest	The rampant barter economy made it possible for Gazprom managers to put together a scheme of complex, non-transparent transactions which were vulnerable to corporate fraud. The problem was that a considerable amount of value was lost in the meantime. This was indicative of the economy as a whole and in relation to the biggest companies like Gazprom and UES.
1.2.2.6 Third Order	Relationship-Based	This is an example of the rampant barter economy as an indicator of the level of corporate fraud. Russian companies often based on personal relationships would stitch together complex transactions between companies, their suppliers, the local tax authorities and other government agencies to pay off debts with goods enterprises produced.

### 12. Yukos (9 separate disputes)

**12.1: (Parallel Coding)** Whalen, (1998e); Whalen, (1998g); Whalen, (1998k); Whalen, (1998m); Whalen, (1998p); Whalen, (1998u); Whalen, (1998y); Whalen, (1998ab); Whalen, (1998ad); 'No Reviews Underway At Yukos Subsidiaries', (1998) **10 articles**

Code	Theme	Notes
1.2	Diversion	Large transactions
1.1 First Order	Management	Management of subsidiaries
1.2.2	Diversion of Claims	Transfer pricing
1.1.6	Control	Consolidation

Second Order		
1.2.2.1 1.1.6.1 Third Order	State Interference	The dispute appears to put the federal government in the role of minority shareholder, battling to maintain the value of its holdings against the actions of a powerful financial-industrial group.
1.2.2.5 1.1.6.5 Third Order	Transactions with Self-Interest	Yukos have been accused of transferring value out of subsidiaries to the holding company through practices such as transfer pricing, whereby a holding company buys crude oil from its subsidiaries at below-market prices and resells it for a hefty profit. Furthermore, this value reducing practice negatively affected the share price of the subsidiaries making the terms of consolidation more favourable for the parent company.
1.2.2.12 1.1.6.12 Third Order	Litigation	The FSC ordered subsidiaries of Yukos to reverse actions that gave their boards of directors too much authority with reference to large transactions (reliance on Russian Joint Stock Company law).

## 12.2: Daigle, (1998a) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Raising capital
1.2.2 Second Order	Diversion of Claims	Share issue
1.2.2.3 Third Order	General Meeting	Proposal to allow board of directors to issue shares was voted down at a shareholders meeting.
1.2.2.5 Third Order	Transactions with Self-Interest	It was alleged that the directors were planning to issue shares in a private placement and take all the shares themselves.

1.2.2.7 Third Order	Self-Enforcement	Minority became suspicious of the proposal and voted it down at a shareholders meeting.
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### 12.3: 'Yukos Investor Threatens Lawsuit', (1998) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Financing.
1.2.2 Second Order	Diversion of Claims	The loan was not used to benefit Yukos' subsidiary.
1.2.2.3 Third Order	General Meeting	There were allegations that a vote authorizing the company to guarantee a \$500 million foreign loan to Yukos violated Russian joint-stock company law.
1.2.2.5 Third Order	Transactions with Self-Interest	Yukos voted in favour of a loan of \$500m that was meant for its subsidiary Samaraneftegaz. However, minority shareholders argued that it was not in the interest of the subsidiary because it would end up with the interest payments and the loan itself. Possibly, the minority were concerned that the money would be siphoned off by the parent company. In formal terms, Yukos could have been regarded as an interested party, yet voted on the resolution regardless.
1.2.2.11 Third Order	Shadow of Enforcement	A minority shareholder threatened legal action.

### 12.4: Aliabyev, (1998o) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Financing.
1.2.2 Second Order	Diversion of Claims	Unfair debt swap harming subsidiary's minority.



1.2.2.5 Third Order	Transactions with Self-Interest	Yukos wanted to write off its debts to Tokobank in exchange for a write-off of Tokobank's debts to two subsidiaries (Tomskneft and Eastern Oil) of the oil major. Although Yukos held a majority stake in the subsidiaries, the move would have violated the rights of the minority shareholders of the two subsidiaries. On the other hand, the subsidiaries had little chance of recovering their debts from the bank.
1.2.2.11 Third Order	Shadow of Enforcement	EBRD used the sell option as leverage in persuading the management of Yukos to come up with a credible restructuring plan.

**12.5:** 'Amoco, Yukos Attempt to Revive Joint Oil Plan', (1998); Whalen, (1998d)

**2 articles**

Code	Theme	Notes
1.1 First Order	Management	Unexpected, one-sided termination of partnership.
1.1.2 Second Order	Ownership	Yukos signed an agreement with Amoco to develop a field in 1993 and together won a tender to secure development rights. Amoco invested more than \$100 million in preliminary development of the field. But later Yukos said that it had no business relationship with Amco.
1.1.2.4 Third Order	Unclear rules	One of the cited reasons for the termination of the partnership was that Amoco's approach to the development of the field was not in Russia's best interests.
1.1.2.10 Third Order	Administrative Levers of the State	Yukos made a surprise announcement that it had 'no business relationship' with Amoco. Later, Yukos had to consider compensating Amoco further to Gore – Chernomirdin talks.

**12.6:** 'Size Won't Make Yuksi World-Class', (1998); Whalen, (1998b) **2 articles**

Code	Theme	Notes
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1.1 First Order	Management	Political differences and ownership disputes as an obstacle to joint venture.
1.1.4 Second Order	Misimplementation	Failure to set up a joint venture.
1.1.4.1 Third Order	State Interference	The joint venture between Yukos and Sibneft was threatened due to (in part) political differences between Khodorkovsky and Berezovsky. The latter irritated the Kremlin with his political manoeuvring.
1.1.4.2 Third Order	Inadequate Information	Sibneft and Yukos were among Russia's most secretive companies with unclear ownership and questionable privatisation history.
1.1.4.10 Third Order	Administrative Levers of the State	The joint venture between Sibneft and Yukos was on its last legs due to political differences. Berezovsky had irritated the Kremlin by his political manoeuvring, while Khodorkovsky preferred to keep low profile.

**12.7: Daigle, (1998d); Whalen, (1998t) 2 articles**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.1 First Order	Management	Managing relations with local stakeholders
1.1.5 Second Order	Taxes	Tax arrears
1.1.5.7 Third Order	Self-Enforcement	Thousands of irate workers and citizens in the Siberian town of Neftegansk blocked Yukos President Sergei Muravlenko and other company officials inside a meeting for 12 hours, demanding local taxes and wages be paid <sup>172</sup> . The incident occurred two months after the parent company announced plans to cut back on production and costs due to low world oil prices.
1.1.5.9 Third Order	Private Enforcement	The town's popular mayor, Vladimir Petukhov, was shot dead as he walked to work. The unsolved crime occurred one month after Petukhov again blamed Yukos for many of the town's woes, and led oil workers and municipal employees in an angry demonstration on the main square to protest months of unpaid wages. When first elected, Petukhov made real strides to improve the town's infrastructure by repaving roads and rebuilding the central market, but a shortage of funds finally pushed him to complain. He and the Nefteyugansk Solidarity union staged a rally outside Yuganskneftegaz headquarters that disrupted the subsidiary's annual shareholder meeting.
1.1.5.10 Third Order	Administrative Levers of the State	The protests were probably organised by the administration of Neftegansk calling on Yukos to pay taxes into the local budget. It has also been alleged that workers did not get paid at Yuganskneftegaz, a claim that was denied by

<sup>172</sup> But according to a Yukos spokesperson, the protest did not include company workers (who had been paid), but only civil service employees angry with the local administration for not paying city wages for four months. Only after 12 hours did they meet with the mayor and union members, finally agreeing to transfer 30 million rubles needed by the local government to pay February wages to city workers.

		Yukos. There were demonstrations and finally after a meeting with the unions, mayor and Yugansk officials, 30 million rubles were transferred to the local budget.
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**12.8: 'Yukos Unit Prepares for Bankruptcy', (1998) 1 article**

Code	Theme	Notes
1.1 First Order	Management	Failure to meet financial obligations.
1.1.5 Second Order	Taxes	Tomskneft owed 400 million rubles (\$21 million at Central Bank rate) in taxes to the federal budget and another 200 million rubles to the local budget and the pension fund. It also owed 300 million rubles to its staff in back wages.
1.1.5.3 Third Order	General Meeting	The Tomsk regional property fund declared illegal a decision taken at Eastern's general shareholders meeting to transfer executive powers to Yukos.
1.1.5.12 Third Order	Litigation	A Yukos spokesman said that the court had ignored a Yukos proposal to cover its subsidiary's debt without giving reasons. Plus, the tax case was awaiting trial at the Tomsk arbitration court.

**12. 9: Kenyon, (1998b) 1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Financing
1.2.2 Second Order	Diversion of Claims	Share issue to minimise value of collateral.
1.2.2.5 Third Order	Transactions with Self-Interest	Menatep defaulted on loan repayment, for which it used 30 percent of Yukos shares as collateral. Later it was decided to dilute the stake of the bank through a share issue.

1.2.2.8 Third Order	Third-Party Enforcement	Rosprom financial-industrial group headed by Mikhail Khodorkovsky (included Menatep and Yukos) pushed for a share issue in Yukos diluting the western bank's stake. However, it appears that the bank had an edge over Yukos since the latter was in need of external finance.
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**18. Transneft:** Aliabyev, (1998e); Peach, (1998c); Peach, (1998d); Peach, (1998p); Peach, (1998s); 'Transneft Investigation', (1998); 'Ugly Games At Transneft Must End', (1998) **7 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Post privatization
1.2.2 Second Order	Diversion of Claims	Management buying shares from employees for very cheap.
1.2.2.2 Third Order	Inadequate Information	Workers were coerced into selling their shares; some were threatened and some were lied to - 'a mixture of threats and misrepresentations'. The actual sale of shares was conducted through murky off shore companies and one British company with an untraceable ownership.
1.2.2.4 Third Order	Unclear Rules	The newly appointed chief was using the prosecutor general's office and the Moscow Arbitration Court to reverse the transactions that resulted in a large number of shares going missing further to a questionable consolidation. The contradictory rulings by the same court added to the uncertainty and hence opened the situation up to various interpretations.

1.2.2.5 Third Order	Transaction with Self-Interest	<p>The former president of Transneft and several of his deputies used company funds to buy shares from employees and then transferred the stock to outside firms that they owned at far below market prices. The scheme transferred 21 percent of Transneft either into a management-owned company or into the hands of untraceable offshore entities.</p> <p>The appraisal of shares was completely flawed. Transneft executives bought nearly 85 percent of the 1.55 million shares distributed among workers for \$60 million. A few months later, according to stock brokers, the market value of this stake reached \$1.5 billion.</p>
1.2.2.7 Third Order	Self-Enforcement	<p>Management used the tactics of intimidation i.e. threats of being fired, refusal to issue ownership certificate, deprivation of social benefits, etc. if the workers refused to sell. In general, those who were charged with the task of retrieving the shares were told to do so by all means possible.</p>
1.2.2.10 Third Order	Administrative Levers of the State	<p>The government turned its attention to the case only after hundreds of lawsuits had been filed by rank-and-file workers against their company. In terms of reversing the transactions, it appears that the new management relied on the legal infrastructure, although it would be logical to conclude, that a great deal of political support was at their disposal, in this case, evident by the Finance Ministry's ruling.</p>
1.2.2.12 Third Order	Litigation	<p>The newly appointed chief of Transneft (Dmitry Savelyev) used the prosecutor general's office and the Moscow Arbitration Court to reverse the transactions that resulted in a large number of shares going missing further to a questionable consolidation. The Finance Ministry ruled in favour of the reversal.</p>

**19. Surgutneftegaz: Peach, (1998q); Peach, (1998i) 2 articles**

Code	Theme	Notes
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1.2 First Order	Diversion	Subsidiaries breaking free from the parent company.
1.2.2 Second Order	Diversion of Claims	Share dilution; transfer pricing through a questionable leasing contract.
1.2.2.2 Third Order	Inadequate Information	Rather than continuing a futile legal battle, Russia's third-largest oil producer decided to sell the subsidiaries. Surgut's remaining interest in Ruchi, Nefto-Kombi, and Krasny Neftyanik was sold off for an undisclosed sum to a group of local 'investors.'
1.2.2.3 Third Order	General Meeting	Nefto-Kombi, a company commanding more than 110 filling stations in St. Petersburg, called an extraordinary shareholders meeting at which an additional equity issuance was approved and Surgutneftegaz was stricken from the charter documents and board of directors. A representative from Surgut was allowed into the meeting, though he was forbidden to participate. The reason: his power of attorney letter was sent to the meeting by fax, an act deemed in violation of AGM procedures devised by Nefto-Kombi officials. Surgutneftegaz's stake in the company was diminished from 42 percent to 11 percent.
1.2.2.5 Third Order	Transactions with Self-Interest	Ruchi, a subsidiary of Surgutneftegas, signed a lease contract that effectively funnelled all profits to the leasee, thereby slowly driving the company into bankruptcy. Whoever signed the contract had the backing of the local administration and criminal underworld and took advantage of complete chaos on the country's political arena. Surgutneftegaz eventually decided to sell a number of its subsidiaries which employed similar tactics of transferring value away from the parent.
1.2.2.8 Third Order	Third-Party Enforcement	Surgut failed to get anywhere with court hearings as they kept being postponed on hair-splitting technicalities. A groups of local investors (St. Petersburg) bought Surgut's remaining interest in three subsidiaries (Ruchi, Nefto-Kombi, and Krasny Neftyanik) for an undisclosed sum. It is clear that the local investors exerted influence over the courts and

		local administration.
1.2.2.9 Third Order	Private Enforcement	Surgut subsidiaries (a batch of oil storage facilities and filling stations as well as an oil refinery in Kirishi), had ties with the criminal underworld. The criminal group had access to the local administration. Surgut's stake in the subsidiaries was diluted by means of the crudest of schemes (bankruptcy, striking parent of the charter, etc.).
1.2.2.10 Third Order	Administrative Levers of the State	Surgutneftegaz failed to keep its subsidiaries because it was useless fighting local courts without the regulatory or political support. The new owners of ex-Surgut subsidiaries on the other hand wanted to create a holding company that would control the regional petrol market: A "Central Fuel Company" for Russia's second city. To garner political support, they proposed that the city administration of St. Petersburg acquire a stake in the new entity; in return the city would have the right to store fuel supplies for free and city officials could fill their tanks at a special rate. One has to wonder whether the stake offered to the city of St. Petersburg is a bribe for the years of "legal assistance" in local courts.
1.2.2.12 Third Order	Litigation	The expropriation of Surgut subsidiaries took place because the local parties – local criminal groups and administration – acted in consortium and had the upper hand over Surgut Holding on their own turf. The case was taken to the St. Petersburg Arbitration Court.

## 20. Tatneft: Peach, (1998r) 1 article

Code	Theme	Notes
1.1 First Order	Management	Financing
1.1.1 Second Order	Bankruptcy	A failure to meet the debt obligation.



1.1.1.6 Third Order	Relationship-Based	Tatneft and a group of Western creditors were engaged in unofficial discussions on debt restructuring.
1.1.1.8 Third Order	Third-Party Enforcement	One of the key enforcement mechanisms was the 'cross default clause' which meant that a failure to meet the debt obligation would result in the immediate claim of all other outstanding debts. This would have led to bankruptcy and deprived Tatneft of an opportunity to access much needed foreign capital in the future.

## 21. Sibneft (3 separate disputes)

### 21.1: (Parallel Coding) Latynina, (1998b) 1 article

Code	Theme	Notes
1.1 First Order	Management	Consolidation
1.1.6 1.1.5 Second Order	Control Taxes	Privatisation, fight for control Privatization led to diminishing taxes paid by the company.
1.1.6.1 1.1.5.1 Third Order	State Interference	The city of Omsk administration attempted to increase its dwindling tax revenues and imposed a 2 percent city tax. This fact forced local companies to re-register outside the city including a number of businesses linked to the governor of Omsk. Sibneft followed others, but the city administration introduced a 35-ruble-per-ton tax on crude oil processed by the refinery.
1.1.6.5 Third Order	Transactions with Self-Interest	Berezovsky paid only \$100 million for the company under the loans-for-shares auction. In 1998 the company was paying far less into the local budget. It was alleged that at that time the company was looted by its new management.

1.1.6.8 Third Order	Third-Party Enforcement	Boris Berezovsky was behind the merger of the Omsk Oil Refinery and Tyumen's Noyabrskneftegaz. This merger led to the emergence of Sibneft which caused damage to the local budget of Omsk and in general made little economic sense.
1.1.6.10 Third Order	Administrative Levers of the State	Consolidation of Sibneft was driven by Berezovsky who enjoyed a great deal of political support. In some instances such consolidation happened at the expense of local budgets but was nevertheless made possibly because of the support of regional administration.
1.1.6.12 1.1.5.12 Third Order	Litigation	Sibneft registered its refinery outside the city of Omsk for tax reasons. The city administration responded by introducing a 35 ruble per ton tax on oil processed by the refinery. Sibneft challenged the tax in courts.

**21.2: (Parallel Coding)** Koriukin, (1998a); Whalen, (1998n); Whalen, (1998o); Whalen, (1998x); 'Yukos Investor Threatens Lawsuit', (1998) **5 articles**

Code	Theme	Notes
1.2 1.2 First Order	Diversion	Share price manipulation
1.2.2 1.2.1 Second Order	Diversion of Claims Diversion of Assets	Closed share issue Sibneft depressed the market price of its subsidiaries on the eve of consolidation.
1.2.2.5 1.2.1.5 Third Order	Transactions with Self-Interest	Sibneft was siphoning off value from its subsidiaries Omsk Oil Refinery and Noyabrskneftegas (e.g. Sibneft purchased oil from Noyabrskneftegas at a below market price driving the stock value down). Once the value of the subsidiaries was low enough, the parent company consolidated the battered subsidiaries at the expense of minority shareholders.

1.2.2.12	Litigation	Minority filed suits in local courts and relied on the ruling of the FSC with regard to what they thought were illegal practices of share dilution by the parent.
1.2.1.12		
Third Order		

**21.3: Whalen, (1998a) 1 article**

Code	Theme	Notes
1.1 First Order	Management	Minority shareholders
1.1.2 Second Order	Ownership	U.S. investor Kenneth Dart was investigated by the State Antitrust Committee which sought to establish whether he colluded with other shareholders to control more than 20 percent of Sibneft's subsidiary Noyabrskneftegaz without permission from the committee. Dart Management provided a compelling argument suggesting why his holding could not have been above the allowed limit.
1.1.2.2 Third Order	Inadequate Information	Dart Management did not publicly disclose its shareholding information.
1.1.2.10 Third Order	Administrative Levers of the State	The investigation was interpreted as a warning to the US investor who became increasingly vocal in his criticism of the Russian investment climate.

**22. Sidanko (5 separate disputes)**

**22.1: 'Sidanko Issue Review?' (1998); Whalen, (1998m); Whalen, (1998e); Whalen, (1998q); Whalen, (1998s); Whalen, (1998z) 6 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Financing
1.2.2 Second Order	Diversion of Claims	Closed bond issue
1.2.2.2	Inadequate Information	The closed bond issue was not advertised to minority when they were buying in.

1.2.2.5 Third Order	Transactions with Self-Interest	The closed bond issue, if went ahead, would have constituted share dilution. Also, there appears to be confusion because at a certain shareholder meeting, a Sidanko's representative was minuted as saying that all subsidiary companies would participate in the bond issue. However, Sidanko intended to sell the bonds to Uneximbank insiders only at about \$1.60 per share, roughly one-tenth the market price of Sidanko stock.
1.2.2.6 Third Order	Relationship-Based	The FSC responded by cancelling the bond issue saying that it may be reregistered if Sidanko was able to form a plan agreeable to minority shareholders. Investor-savvy Uneximbank was predicted to make peace with its shareholders and to ensure that investors did not lose money in the bond issue. There were private negotiations between Uneximbank and investors about solving the problem to the satisfaction of both parties.
1.2.2.7 Third Order	Self-Enforcement	The minority complained about the closed bond issue. The parent company had to negotiate with the disgruntled shareholders as it was seeking to improve its corporate governance image.
1.2.2.10 Third Order	Administrative Levers of the State	Sidanko's bond issue which included an interested-party transaction was investigated by the FSC. The investigation came further to a complaint from former Finance Minister Boris Fyodorov raising questions about the legality of the issue. At the time the regulators and politicians were concerned over the country's investment image.
1.2.2.12 Third Order	Litigation	The securities commission headed by Vasiliev (further to finance minister Boris Fyodorov's written complaint), cancelled the bond issue that diluted the stake of minority by limiting the issue to two parties. The securities commission said that it would allow the bond issue provided a mutually acceptable solution was found.

**22.2:** 'Sidanko Tells State To Rethink Oil Cuts', (1998); 'Sidanko to Honor Tax Debts But Complains Bill Is Inflated', (1998); 'Sidanko, Onako Warned on Debts', (1998); 'Sidanko Unit Goes Bankrupt', (1998); **4 articles**

Code	Theme	Notes
1.1 First Order	Management	Financing
1.1.5 Second Order	Taxes	Non-payment of taxes
1.1.5.1 Third Order	State Interference	The government cut Sidanko's access to the export pipeline by a third because the company failed to meet tax payments. At the time, the state was having difficulty raising the revenues needed to provide basic services and to pay millions of state workers on a timely basis.
1.1.5.10 Third Order	Administrative Levers of the State	Under a government resolution, the ministry could cut access to export pipelines for companies that were behind with their tax dues.

**22.3: (Parallel Coding): Whalen, (1998r); Whalen, (1998l) 2 articles**

Code	Theme	Notes
1.1 First Order	Management	Non-payment in the local budget.
1.1.6 1.1.5 Second Order	Control Taxes	Regional administration taking control over Sidanko's subsidiary which failed on tax payments.
1.1.6.1 1.1.5.1 Third Order	State Interference	The company was fighting local administration with regard to back tax claims against its subsidiary (the Angarsk refinery). Bankruptcy proceedings were initiated by the local court taking control of the cash flow of the refinery away from Sidanko. In response Sidanko stopped shipments of crude oil. The move infuriated the local and federal governments.
1.1.6.10 1.1.5.10 Third Order	Administrative Levers of the State	The Irkutsk regional administration attempted to usurp control of a Sidanko's subsidiary by pushing for bankruptcy for non-payment of taxes. There is a contradiction of business and political objectives where the priority is on keeping a loss making entity in operation for continuous employment in the region.  Sidanko did not fight till the end since it did not consider the subsidiary of much value.
1.1.6.12 1.1.5.12 Third Order	Litigation	Irkutsk regional administration sought to take control over the refinery on the back of tax allegations by installing external managers further to a ruling made by the regional arbitration court.

**22.4: Kenyon, (1998a); 'Sidanko Unit Goes Bankrupt', (1998) 2 articles**

Code	Theme	Notes
1.1	Management	Management of the subsidiaries.

First Order		
1.1.1 Second Order	Bankruptcy	Bankruptcy was called for by the creditors and objected to by the majority shareholder.
1.1.1.5 Third Order	Transactions with Self-Interest	Creditors of a Sidanko's unit Kondpetroleum decided to call for bankruptcy alleging a continuous transfer of value from the daughter company to the parent. Sidanko opposed the local court's decision to appoint a special (bankruptcy) manager.
1.1.1.12 Third Order	Litigation	The court ruled in favour of the creditors who were calling for bankruptcy.

**22.5: (Parallel Coding) Aliabyev, (1998f); Whalen, & Korchagina, (1998) 2 articles**

Code	Theme	Notes
1.1 First Order	Management	Dealing with creditors and competitors.
1.1.6 1.1.1 Second Order	Control Bankruptcy	Bankruptcy proceedings were used in order to gain control of Chernogorneft.
1.1.6.6 1.1.1.6 Third Order	Relationship-Based	It is unclear why the two creditors who were left out from the bankruptcy proceedings did not react to the news. It was speculated that a behind the scenes agreement had been formed.
1.1.6.8 1.1.1.8 Third Order	Third-Party Enforcement	It is possible that Sidanko's competitors (either Surgutneftegaz or Tyumen Oil Co.) were behind the bankruptcy proceedings of Chernogorneft. The idea was to capitalize on a perfectly viable company's woes. It demonstrates the weakness of the legal system. Two foreign investors, who reportedly held 60 percent of Chernogorneft's \$133 million total debt, were not included on the list of creditors who stood to benefit from

		Chernogorneft's possible bankruptcy.
1.1.6.12 1.1.1.12 Third Order	Litigation	It appears that courts were used as the main mechanism of enforcement. A number of creditors were excluded from the bankruptcy proceedings. It is possible that the court excluded the creditors on technicalities such as an application not being filed in time, or register entries not being properly checked. It is also possible that Sidanko's competitors were behind the bankruptcy proceedings.

**23. Tyumen Oil Co.:** Interfax & MT (1999); Reuters & Itar-Tass (1998); Whalen, (1998h); Whalen, (1998i); Whalen, (1998v); Whalen, (1998w); Whitehouse, (1998e) **7 articles**

Code	Theme	Notes
1.1 First Order	Management	Renegade director.
1.1.6 Second Order	Control	The renegade director used the support of the workers' collective of the subsidiary in order to maintain his control of Nizhnevartovsk.
1.1.6.5 Third Order	Transactions with Self-Interest	It was suggested that the terms of the privatisation tender were rigged in Alfa's favour. Alfa won a privatization tender, paying only \$810 million for the 40 percent share in Tyumen. As a result of that, Nizhnevartovskneftgaz rebelled and refused to hand control over until an out-of-court settlement was reached. It is unclear whether the renegade director acted on behalf of the workers union or in self-interest.



1.1.6.6 Third Order	Relationship-Based	The fight for control made it difficult for Tyumen to raise financing, slowed Nizhnevartovskneftegaz's oil exports to a trickle and left Tyumen's Ryazan refinery without a crude oil supplier. In the end, the two parties reached an out-of-court settlement.
1.1.6.8 Third Order	Third-Party Enforcement	Paly allegedly transferred stakes in daughter companies to off-shore accounts in order to have financial leverage as a means of protection from the powerful industrial groups. Eventually he gave up or was bought by the FIGs i.e. Alfa and Renova. The parties to the conflict were interested in a speedy resolution, because the parent (Tyumen) and the subsidiary (Nizhnevartovskneftegaz) were losing money.
1.1.6.10 Third Order	Administrative Levers of the State	The government intervened with a warning urging the renegade director and Alfa to reach a compromise.
1.1.6.12 Third Order	Litigation	A Federal Arbitration Court ruled in favour of replacing Paly with a Tyumen official if bankruptcy was to be avoided.

**24. Krasnoyarsk Hydro: (Parallel Coding) Aliabyev, (1998p); Baker-Said, (1998); Daigle, (1998c); 'Hydro Plant Share Issue', (1998) 4 articles**

Code	Theme	Notes
1.2 1.1 First Order	Diversion Management	Transaction involving a purchase of a significant stake.
1.2.2 1.1.6 Second Order	Diversion of Claims Control	Fight for control and diversion of claims.
1.2.2.3 1.1.6.3 Third Order	General meeting	It was alleged that Krasnoyarskenergo's chief executive, Vladimir Kolmogorov, was not allowed to vote the company's 28 percent stake in the power plant because he was chosen at a shareholders meeting that was

		declared invalid by a local court. KrAZ denied that there had been any irregularities at the shareholders meeting.
1.2.2.5 1.1.6.5 Third Order	Transactions with Self-Interest	Siberian hydroelectric station Krasnoyarsk Krasnoyarskenergo, which was controlled by UES, sold a 23 percent stake in the hydroelectric power station Krasnoyarsk Hydro to Tanako, a financial industrial group established by Krasnoyarsk Aluminum or KrAZ. The sale reduced Krasnoyarskenergo's stake in the power plant to 28 percent. It was claimed that the stake had been sold at a fraction of its real value.
1.2.2.7 1.1.6.7 Third Order	Self-Enforcement	In the end, the UES signed a share management deal because it felt that it would not be possible for it to regain control of the plant.
1.2.2.8 1.1.6.8 Third Order	Third-Party Enforcement	Krasnoyarskenergo, which was controlled by UES sold a 23 percent stake in the hydroelectric power station to Tanako, a financial industrial group established by Krasnoyarsk Aluminum or KrAZ. The sale reduced Krasnoyarskenergo's stake in the power plant to 28 percent. UES ousted Krasnoyarskenergo's general director, Vladimir Ivannikov, who oversaw the deal.
1.2.2.10 1.1.6.10 Third Order	Administrative Levers of the State	Nemtsov denounced the sale saying that the stake was sold for a fraction of its value. This battle ran parallel to the highly political battle at the top of UES between Dyakov and Brevnov.
1.2.2.12 1.1.6.12 Third Order	Litigation	The Tanako FIG exerted pressure on the management of Krasnoyarskenergo to sell the stake in Krasnoyarsk Hydro for cheap. UES mounted a legal challenge in an effort to return the stake. Secondly, the increase of authorised capital of Krasnoyarsk Hydro was voted by the shareholders, but the FSC announced an investigation into the rights issue and the legitimacy of the shareholder meeting.

## 25. UES (4 separate disputes)

**25.1:** Aliabyev, (1998c); Baker-Said, (1998a); Baker-Said, (1998b); Baker-Said, (1998e); Baker-Said, & Zaks, (1998); 'Challenge To Brevnov Is Senseless', (1998); 'Duma Launches Attack on Brevnov', (1998); Latynina, (1998a); Lowe, (1998); Peach, (1998f); Whalen, (1998c) **11 Articles**

Code	Theme	Notes
1.1 First Order	Management	Highly political and lacking business rationale.
1.1.6 Second Order	Control	Fight for control.
1.1.6.1 Third Order	State Interference	A fight between Chernomyrdin (Prime Minister) and Nemtsov (Deputy Prime Minister) filtered down to a fight between Dykov and Brevnov. Both parties relied on various powerful establishments while accusing each other of corruption.
1.1.6.5 Third Order	Transactions with Self-Interest	There were allegations of transactions involving the company's veksel designed to transfer value away from UES for the benefit of management. Plus questionable loans, barter schemes and extravagant expense claims.
1.1.6.6 Third Order	Relationship-Based	Brevnov was Nemtsov's friend while Dyakov was supported by Chernomyrdin.
1.1.6.10 Third Order	Administrative Levers of the State	Both clans relied heavily on various institutions at their disposal like the Account Chamber and State Duma.
1.1.6.11 Third Order	Shadow of Enforcement	Lots of warnings and political rhetoric aimed at frightening the sides into surrender.

**25.2:** Baker-Said, (1998c); 'Chubais Not Right Man For UES Job', (1998); Whalen, (1998c); Whitehouse, (1998b) **4 articles**

Code	Theme	Notes
1.1 First Order	Management	Nominations
1.1.6 Second Order	Control	The question who would head UES was decided through political support and crony

		agreements.
1.1.6.5 Third Order	Transactions with Self-Interest	Allegedly, Chubais received bribes and promises of high-ranking positions for privatisation favours.
1.1.6.6 Third Order	Relationship-Based	Chubais was supported because of his contacts with Western banks. Also, the privatisation deals required a great deal of personal trust.
1.1.6.10 Third Order	Administrative Levers of the State	Influential politicians relied on power structures at their disposal in order to pursue their self-centred means.
1.1.6.12 Third Order	Litigation	A Moscow district court rejected a libel suit he filed against a Russian investigative journalist and a Moscow radio station that accused Chubais of accepting a \$90,000 bribe in a fake book deal.

### 25. 3: Berezanskaya, (1998b) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Distribution of residuals.
1.2.2 Second Order	Diversion of Claims	Promised dividends were not paid
1.2.2.11 Third Order	Shadow of Enforcement	The National Reserve Bank said it was preparing legal action against Unified Energy Systems for failure to pay promised 1996 dividends. Bank chairman Alexander Lebedev said at a news conference that he will wait and see whether new management at UES agrees to pay the money.

**25. 4:** Aliabyev, B. (1998k); Baker-Said, S. (1998c); Baker-Said, S. (1998h); 'Bill on UES Saps Russia's Credibility', (1998); 'Duma Vote Likely to Scuttle Plans for Sale of UES Stake', (1998); Rao, S. (1998h); 'UES Halts Trading In ADRs', (1998); 'Yeltsin Aide Blasts Law On UES', (1998) **8 articles**

Code	Theme	Notes
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1.1 First Order	Management	Ownership restriction.
1.1.2 Second Order	Ownership	The law passed by the Duma, the lower chamber of parliament, required the government to keep a 51 percent stake in UES, which controlled 75 percent of Russia's electricity. Foreign ownership was limited to 25 percent despite foreigners owning more than 28 percent of the company.
1.1.2.1 Third Order	State Interference	The law was the result of tensions between Yeltsin and the Communist-dominated Duma over the Cabinet shake-up, and a shake-up in the management of UES.
1.1.2.4 Third Order	Unclear Rules	The law limited foreign ownership to 25 percent despite the fact that foreigners had already acquired almost 30 percent. There was no plausible mechanism for compensating foreigners
1.1.2.10 Third Order	Administrative Levers of the State	The law was a part of political bargaining over who would be appointed as the prime minister.
1.1.2.12 Third Order	Litigation	The chairman of the UES board of directors, Viktor Kudryavy, said that the bill infringed on the rights of shareholders and would be impossible to enforce. Yeltsin was expected to appeal the content of the law in the Constitutional Court.

## 26. Mosenergo: Aliabyev, (1998i) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Share issue.
1.2.2 Second Order	Diversion of Claims	Because Mosenergo purchased plants from 'friendly' UES, a damaging insider dealing practice was suspected.
1.2.2.3 Third Order	General Meeting	The decision on share issue was made at the shareholders meeting. Because the decision made economic sense, it was approved. However, the existing stakes of minority shareholders were diluted.

1.2.2.5 Third Order	Transactions with Self-Interest	Dilution of the foreign investors' stake from 29 percent to 25.5 percent.
1.2.2.7 Third Order	Self-Enforcement	The shareholders reached consensus even though a certain minority stood to lose out as a result of the rights issue.

## 27. Electrosila: Varoli, (1998) 1 article

Code	Theme	Notes
1.1 First Order	Management	Balancing the interests of shareholders.
1.1.6 Second Order	Control	Majority shareholder decided that the existing director was no longer suitable for them. It was speculated that the director needed to be replaced with someone who would be more active at recovering a lost stake on behalf of a majority shareholder (EMK). Siemens protested saying that they were happy with the existing director who returned Elektrosila to profitability.
1.1.6.4 Third Order	Unclear Rules	EMK, majority shareholder in Elektrosila, ignored the decision of the court and installed a new director who was working alongside the old one.
1.1.6.8 Third Order	Third-Party Enforcement	Most analysts suggested that Siemens will lose because EMK is a majority shareholder and a powerful corporation.
1.1.6.12 Third Order	Litigation	When the existing director was replaced, Siemens took the case to court and received a ruling in its favour (the decision to replace the director was in violation of the company's charter). EMK, majority shareholder in Elektrosila, ignored the decision of the court.

## 28. Norilsk Nickel (3 separate disputes)

### 28.1: 'Duma Asks for Sell-Off Reversal', (1998) (1 article)

Code	Theme	Notes
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1.1 First Order	Management	Legitimacy of privatisation was questioned
1.1.2 Second Order	Ownership	The results of high profile privatization deals were threatened to be reversed.
1.1.2.5 Third Order	Transactions with Self-Interest	Under the loan-for-shares scheme, the government received money from Russian banks against stakes in Russia's most attractive state-owned companies. The loans were never repaid, and the banks acquired the stakes for prices far-below market value. Norilsk Nickel was privatised by means of this arrangement.
1.1.2.10 Third Order	Administrative Levers of the State	The government was on the verge of bankruptcy and was very much dependant on financial structures that had all the bargaining power on their side. Analysts suggested that the review of the loan-for-shares deals was unlikely because of the involvement of the powerful financial industrial groups.
1.1.2.12 Third Order	Litigation	The fact that Duma voted unanimously in favour of the reversal through courts indicated a great deal of public dissatisfaction with the loan-for-shares deals.

**28.2: 'Share Issue Gives Norilsk \$400M', (1998) 1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Share Issue
1.2.2 Second Order	Diversion of Claims	Diversion of claims through exclusion of a group of shareholders from a share issue.
1.2.2.2 Third Order	Inadequate Information	The company failed to ensure that all preferred stock was transferred into ordinary stock; a condition upon which most institutional investors had bought into the preferred stock. Furthermore, Uneximbank later relented and changed the terms of the issue, but investors who sold their stock on the false news lost out.

1.2.2.5 Third Order	Transactions with Self-Interest	Norilsk announced its intention to double its charter capital with the issue of a further 126 million shares. The first plan it drafted was scrapped because it was perceived to exclude preferred shareholders.
1.2.2.7 Third Order	Self-Enforcement	The company was forced to change the terms of the new share issue because the losing party i.e. preferred shareholders; (mainly institutional investors) started dumping their holdings, thereby driving the preferred share price down by some 10 percent. However, the new issue was on slightly less favourable terms, i.e. the price of the issued stock was higher.

**28.3: 'Norilsk Nickel Fights State Over Tax-Owing Subsidiary', (1998) 1 article**

Code	Theme	Notes
1.1 First Order	Management	Managing relations with the government.
1.1.5 Second Order	Taxes	Back taxes claim leading to the government pressing for bankruptcy proceedings against a subsidiary.
1.1.5.1 Third Order	State Interference	The government had to boost tax collection in order to close a substantial budget deficit. In this particular case the decision was made to recover some of the tax debt through bankruptcy of a Norilsk Nickel's subsidiary.
1.1.5.12 Third Order	Litigation	The government, under a great deal of pressure from western investors to improve tax collection, pressed for Severonickel's bankruptcy because, apparently, the subsidiary had a substantial tax debt. Norilsk Nickel appealed the decision in an arbitration court arguing that the tax debt of \$40 million was calculated incorrectly.



## 29. Novolipetsk (2 separate disputes)

**29.1:** Baker-Said, (1998f); Borisova, (1998d); Whitehouse, (1998e); Whitehouse, (1998g)  
**4 articles**

Code	Theme	Notes
1.1 First Order	Management	Board representation.
1.1.6 Second Order	Control	Fight for control; 40 percent minority was blocked from getting a proportionate board representation.
1.1.6.3 Third Order	General Meeting	Once a court returned the ruling in favour of the minority shareholders, the old management attempted to avoid allowing the shareholders to vote in their representatives by removing voting from the agenda of the shareholders meeting.
1.1.6.4 Third Order	Unclear Rules	There were a number of conflicting decisions that the Lipetsk arbitration court returned, and at some point there was a decision to take the case to the Supreme Arbitration Court.
1.1.6.12 Third Order	Litigation	Clearly the minority shareholders relied on courts which eventually ruled in their favour.

**29.2: (Parallel Coding):** Baker-Said, (1998f); Borisova, (1998d); Rao, (1998b)

**3 articles**

Code	Theme	Notes
1.2	Diversion	Insider dealing
1.1 First Order	Management	Squeezing out an unwanted shareholder
1.2.2	Diversion of Claims	Diversion of claims through alleged insider dealing.
1.1.6 Second Order	Control	Forcing an unwanted shareholder to sell their stake.

1.2.2.5 1.1.6.5 Third Order	Transactions with Self-Interest	Trans-World Group, which had about 35 percent of stock at the combine, was buying metal cheaply at the NLMK to resell it on the London commodity market at a profit. This made other shareholders unhappy.
1.2.2.7 1.1.6.7 Third Order	Self-Enforcement	The new shareholders blocked Trans-World's vote and by doing so, forced the company to sell its stake.
1.2.2.8 1.1.6.8 Third Order	Third-Party Enforcement	The financial groups behind the new shareholders squeezed Trans-World out by means of blocking its vote. It appears that the interest in Novolipetsk arose as a result of rosy forecasts for the industry.
1.2.2.10 1.1.6.10 Third Order	Administrative Levers of the State	The State Duma's security committee launched an attack against Trans-World, alleging its director, Briton David Reuben, was a spy. The investigation by the State Duma securities commission of the Trans-World Director must have been a coordinated effort (rather than a coincidence) in driving the British company away from the dominant position in the industry.
1.2.2.12 1.1.6.12 Third Order	Litigation	The British company filed a number of cases in European courts with a Dutch court ruling in its favour ordering seizure of Novolipetsk's metal in Rotterdam in Trans-World's favour.

### 33. Magnitogorsk: Aliabyev, (1998d); Aliabyev, (1998m); Aliabyev, (1998n)

#### 3 articles

Code	Theme	Notes
1.1 First Order	Management	Negotiating with external finance providers.
1.1.2 Second Order	Ownership	Ownership dispute in which the company that managed shares refused to hand in the shares that were meant to be used as collateral for a loan from the EBRD. The loan was meant to modernise the plant, but the collateral would have changed the ownership structure.

1.1.2.2 Third Order	Inadequate Information	The company ousted the renegade director for his refusal to hand over the shares. However, the shares were hidden in a number of transactions involving undisclosed foreign companies and individuals.
1.1.2.4 Third Order	Unclear rules	<p>The company ousted the renegade director for his refusal to hand over the shares. However, the shares were hidden in a number of transactions involving undisclosed foreign companies and individuals. These transactions were made possible by the local share registrars who approved the transactions after the court order had frozen the disputed shares.</p> <p>Moreover, there was additional confusion, because the two parties to the conflict held their own board meetings since a Moscow district court returned a ruling reinstating Sharipov in his previous position.</p>
1.1.2.5 Third Order	Transactions with Self-Interest	The company that was appointed to manage shares of Magnitogorsk may have resisted the hand over of shares as collateral for the loan because the stake represented its main asset. Consequently, the shares changed hands in a number of transactions involving undisclosed foreign companies and individuals.
1.1.2.7 Third Order	Self-Enforcement	Sharipov encouraged a number of transactions involving foreign partners and the local share registrar to hide the shares. He explained his actions by suggesting that handing over the shares would lead to a redistribution of property.
1.1.2.8 Third Order	Third-Party Enforcement	The plant depended on the finance from the EBRD and possibly was prepared to accept less favourable terms. Bearing in mind the difficult financial situation in the country, the chances of the plant failing on repayment terms must have been fairly high.

1.1.2.10 Third Order	Administrative Levers of the State	The new management acted on the directions of the central government that clearly supported the loan.
1.1.2.12 Third Order	Litigation	The dismissal was fought in a Moscow district court. There were criminal charges against Sharipov for his failure to follow an earlier court order compelling him to hand over the shares. The Federal Securities Commission closed down the local registrar that authorised the deals with the disputed shares. However, a Moscow Court reinstated Sharipov to his position further to the sacking.

### 34. Lebedinsky Ore Mining Plant (2 separate disputes)

#### 34.1: Borisova, (1998a); Todres, (1998) 2 articles

Code	Theme	Notes
1.1 First Order	Management	Privatisation.
1.1.2 Second Order	Ownership	Ownership dispute regarding a 10 percent stake that had been sold on the back of legal confusion, hence in part constituting a diversion of claims.
1.1.2.1 Third Order	State Interference	The government attempted to return the lost stake through the courts. It failed to achieve its task of maximizing revenue from the auction of the stake as during the time of the dispute a majority shareholder emerged that scared off minority investors.
1.1.2.4 Third Order	Unclear Rules	The court system produced two contradictory rulings complicating the situation. Finally, the government suggested that although the present stock holders obtained the shares legitimately, it was not theirs as in the past, i.e. the disputed stock was sold improperly.
1.1.2.5 Third Order	Transactions with Self-Interest	Those who attempted to hide the stakes did so by selling it to a foreign company which possibly was closely affiliated to Russian partners.

1.1.2.8 Third Order	Third-Party Enforcement	The whole pursuit of shares might have been caused by the pressure from the IMF that was calling for greater effort to collect money on the part of the Russian government.
1.1.2.10 Third Order	Administrative Levers of the State	It might have been that the fate of the stakes had already been decided (amongst government officials or well connected insiders) away from the spotlight and the government was just keen to demonstrate the illusion of the action that was doomed to fail. It is entirely possible that the government exerted pressure on the legal system to come up with the rulings in its favour at the required time.
1.1.2.12 Third Order	Litigation	There was an overall reliance on courts in the government's pursuit of the lost stake. The government clearly wanted to see the stake returned (or create an illusion to that effect) and eventually, the Moscow court ruled in the government's favour.

#### 34.2: Borisova, (1998a) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Unwanted shareholder.
1.2.2 Second Order	Diversion of Claims	Diversion of claims through illegal increase of the company's charter capital.
1.2.2.5 Third Order	Transactions with Self-Interest	Lebedinsky Ore Mining Plant's management tried to dilute the stake of Rossiisky Kredit by illegally increasing the charter capital. Rossiisky Kredit managed to hold its ground, but made enemies with the local administration and the plant's management. When Rossiisky Kredit incurred liquidity problems brought about by the crisis, the bank was forced to sell its stake to Nacosta.

1.2.2.10 Third Order	Administrative Levers of the State	The plant's management and local administration used vulnerability of Rossiisky Kredit (caused by the looming crisis) to squeeze out the bank from the list of its shareholders. With regard to the charter capital increase, the parties used their proximity to local courts and other institutions in the Belgorod region to fight the bank.
1.2.2.12 Third Order	Litigation	With regard to the increase of the charter capital, there was some reliance on courts that helped Rossiisky Kredit hold its ground.

**35. Achinsk Alumina Combine: (Parallel Coding) Aliabyev, & Koriukin, (1998) article**

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Code	Theme	Notes
1.1 First Order	Management	Shortage of finances
1.1.1 1.1.3 1.1.6 Second Order	Bankruptcy Misinvestment Control	The debt laden plant was allegedly protected from bankruptcy because the local administration was trying to prevent the plant's collapse due to far reaching social implications. There was a fight for control of the plant between the local administration and creditor.
1.1.1.4 1.1.3.4 1.1.6.4 Third Order	Unclear Rules	Every twist of the dispute around the combine and possible bankruptcy followed a change of Lebed's stand on the issue. I was alleged that Lebed withdrew his support of Kraz in favour of Alfa and vice versa.
1.1.1.6 1.1.3.6 1.1.6.6 Third Order	Relationship-Based	Had Alfa (Alfa-Eko, a part of Alfa group and a major creditor of the combine) sided with Lebed, the local governor, the resolution, surely, would have been different. KRAZ, on the other hand managed to reach some sort of a compromise with the local administration (probably on a private level).
1.1.1.8	Third-Party	Had Alfa sided with Lebed, the local governor, the resolution, surely, would have been

1.1.3.8 1.1.6.8 Third Order	Enforcement	different. KRAZ, on the other hand managed to reach some sort of a compromise with the local administration.
1.1.1.10 1.1.3.10 1.1.6.10 Third Order	Administrative Levers of the State	The creditors should have had the upper hand, but the support of the local administration must have been decisive in the rulings of the local courts.
1.1.1.12 1.1.3.12 1.1.6.12 Third Order	Litigation	There was an overall reliance on courts in the pursuit of control over the debt laden plant. However, it appears that the final call on the issue was made by the local governor and the financial group behind him. It is clear that the local administration was critical in ensuring that KRAZ maintains control over the debt laden plant. From this, it is once again evident that the local courts were very much under control of the local administration.

### 36. Knauf (2 separate disputes)

#### 1. (Parallel Coding): Daigle, (1998b) 1 article

Code	Theme	Notes
1.1 First Order	Management	New investor fighting local stakeholders.

1.1.6 1.1.2 Second Order	Control Ownership	Sergiyenko (appointed director) was suspended from office on allegations of theft, mismanagement and tax manipulation. His response was to hold his own meetings, remove Knauf from the company's name, and issue 64 percent new shares to dilute the Germans' stake.
1.1.6.3 1.1.2.3 Third Order	General Meeting	Sergiyenko's response was to hold his own meetings, remove Knauf from the company name, and issue 64 percent new shares to dilute the Germans' stake.
1.1.6.5 1.1.2.5 Third Order	Transactions with Self-Interest	Sergiyenko removed Knauf from the company name, and diluted the Germans' stake.
1.1.6.7 1.1.2.7 Third Order	Self-Enforcement	Knauf, as the rightful owner of the Kubansky Gyps-Knauf gypsum mine refused to leave the office as the renegade director attempted to seize control over the company. The Germans barricaded themselves in the building believing that physical possession was more valuable than meaningless court orders.
1.1.6.9 1.1.2.9 Third Order	Private Enforcement	Sergiyenko used the support of the local government and Cossack Army to oust Knauf officials, while the German company appealed to the federal government for support.
1.1.6.10 1.1.2.10 Third Order	Administrative Levers of the State	The local authorities supported the coup arguing that the plant should be renationalised while the federal government, although inactive, was on Knauf's side.
1.1.6.12 1.1.2.12 Third Order	Litigation	30 court decisions were ignored. However, eventually, commission for the protection of investor rights resolved the dispute in favour of Knauf.

### 36.2: (Parallel Coding) Whalen, (1998f) 1 article

Code	Theme	Notes
1.1	Management	Relations with local stakeholders.



First Order		
1.1.5 1.1.6 Second Order	Taxes Control	Although tax police were formally right as Knauf made an accounting mistake, the former refused to consider the evidence (receipts) supplied by Knauf.
1.1.5.5 1.1.6.5 Third Order	Transactions With Self-Interest	It appears that an unidentified party was using tax authorities to exert pressure on the company to either surrender control, or simply share profits.
1.1.5.8 1.1.6.8 Third Order	Third-Party Enforcement	An unidentified party was behind the allegations against Knauf.
1.1.5.12 1.1.6.12 Third Order	Litigation	The arbitration courts ruled in favour of the decision made by the tax authorities.

### 38. AssiDoman (2 separate disputes)

#### 38.1: Aliabyev, (1998b); Aliabyev, (1998j) 2 articles

Code	Theme	Notes
1.1 First Order	Management	Pre foreign investment debts.
1.1.5 Second Order	Taxes	Back taxes and pension arrears.
1.1.5.6 Third Order	Relationship-Based	The company sought to establish personal relationships with key individuals in the position of power like Chubais and Mostovi. Their efforts were cancelled out by the reshuffle. The company raised its hopes on a new person (Nemtsov) but as a precaution ceased production while negotiating with the authorities and major shareholders.

1.1.5.10 Third Order	Administrative Levers of the State	It appears that Yeltsin's comments were not taken too seriously, as his pledges to help did not sound convincing enough for the company to restart capital investments and production. Meanwhile, the tax authorities froze the company's accounts.
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**38.2:** Aliabyev, (1998a); Aliabyev, (1998b); Aliabyev, (1998g); Aliabyev, (1998j)

'AssiDoman Pulls Out', (1998); Schwartz, (1998e); **6 articles**

Code	Theme	Notes
1.1 First Order	Management	Legitimacy of the purchased assets.
1.1.2 Second Order	Ownership	The legitimacy of the ownership stake was thrown into question because of unclear rules of the game, while minority shareholders with powerful backing sought to capitalise on the situation.
1.1.2.4 Third Order	Unclear Rules	AssiDoman purchased a stake in a paper mill. It is possible that the legality of this purchase was questioned because someone else became interested in the stake. The courts were used to challenge the legitimacy of the stake. Subsequently, AssiDoman expressed a wish to sell its stake saying that it had underestimated problems with Russian bureaucracy.
1.1.2.8 Third Order	Third-Party Enforcement	It is unclear why AssiDoman's stake was questioned by the courts. The only reasonable explanation would be an effort from either a minority shareholder or a Third-Party to win over control and ownership of the paper mill.
1.1.2.10 Third Order	Administrative Levers of the State	Despite pledges from high ranking officials, including Boris Yeltsin, the government refused to offer the \$60m guarantee without the backing of the Karelian government and the all clear from the courts. That fact prevented a sustained inflow of cash from AssiDoman. There were worthless pledges of support from the central government which

		was clearly incapable of enforcing decisions on the minority shareholders which enjoyed the support of the local administration.
1.1.2.12 Third Order	Litigation	The State Anti Trust Committee's decision to allow the transfer of the stake to AssiDoman was declared illegal by the Moscow Arbitration Court. AssiDoman issued a statement in which it confessed that the problems with partners and bureaucracy had been underestimated.

**39. Vyborg Paper: (Parallel Coding)** Lagnado, (1998a); Digges, (1998); Lagnado, (1998b) **3 articles**

Code	Theme	Notes
1.1 First Order	Management	Maintaining relationships with stakeholder, i.e. employees.
1.1.2  1.1.4 Second Order	Ownership/ Misimplementation	Fight for control and ownership which resulted in a failure to implement what otherwise would have been a viable project
1.1.2.7 1.1.4.7 Third Order	Self-Enforcement	The trade unions, encouraged by national attention and political support, organised strikes, seizure of the mil, and blockage of the motorway. In the end the government decided to re-nationalise the property and thus supported employees in their efforts to return the paper mill.

1.1.2.10 1.1.4.10 Third Order	Administrative Levers of the State	A promise to settle taxes and not lay off employees was broken by Nimonor (a company that was registered three weeks prior to the sale of the mill). The company tried to win control over the paper mill by registering an off-shore company, and allegedly by being in cahoots with the local authorities. In the end, the government decided to re-nationalise the property and supported employees in their efforts to return the paper mill.
1.1.2.12 1.1.4.12 Third Order	Litigation	Nimonor failed to honour the agreement to settle wage and tax arrears provoking overreaction from the unions. There was some reliance on the St. Petersburg Arbitration Court in the resolution of this dispute. Also, the parliament responded to the pledges from the workers who received official support from the government.

#### 40. SBS Agro (3 separate disputes)

40.1: '2 Banks Attack Lehman Brothers', (1998); Bershidsky, (1998a); 'SBS-Agro Assets Frozen', (1998); 'Western Banks Drop Bond Lawsuit', (1998) **4 articles**

Code	Theme	Notes
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1.2 First Order	Diversion	Financing
1.2.2 Second Order	Diversion of Claims	Default on payment to foreign investors
1.2.2.10 Third Order	Administrative Levers of the State	SBS Agro complained to the Russian government and insisted on exclusion of Lehman Brothers' from participating in the debt-restructuring process.
1.2.2.12 Third Order	Litigation	Further to the London court decision (a case initiated by Lehman Brothers), the accounts of SBS Agro were frozen. Also, Russian courts made a precedent setting decision on Tokobank which suggested that recovering investments in the banking sector on Russian soil would be very difficult. As far as freezing foreign accounts of Russian banks by foreign courts was concerned, there was a clear lack of enforcement powers over the Russian banks as their deposits in overseas accounts were smaller than their debt.

**40.2:** Korchagina, (1998); 'No SBS-Agro Payments', (1998); Peach, (1998o); Rao, (1998f); 'Sberbank to Release SBS Savings Friday', (1998); **5 articles**

Code	Theme	Notes
1.1 First Order	Management	Lack of money.
1.1.1 Second Order	Bankruptcy	Possible bankruptcy proceedings further to a failure to pay depositors.
1.1.1.4 Third Order	Unclear Rules	Although the Central Bank had said SBS-Agro depositors could have access to their funds, it later retracted that pledge.  At some point due to lack of cash, the bank decided to pay depositors on the basis of their needs. This was an arbitrary approach open to abuse.

1.1.1.10 Third Order	Administrative Levers of the State	Simultaneously, questions were raised as to the legitimacy of the privatization of the bank which was seen as an insider deal involving government officials.
1.1.1.12 Third Order	Litigation	There was a danger of bankruptcy proceedings further to the bank's failure to pay depositors. A Russian court taking a formal stance on the issue froze accounts of the bank. Further bankruptcy proceedings were possible if the bank failed to demonstrate that the money was coming in. Although every precaution not to bankrupt the bank was evident, it had been proposed by the courts that bankrupting might lead to a higher chance of depositors being repaid. In any case, it had also been suggested that depositors with a court order, if not guaranteed, had a better chance of recovering their money than those without.

#### 40.3: Borisova, (1998f) 1 article

Code	Theme	Notes
1.1 First Order	Management	Importance of political connections
1.1.3 Second Order	Misinvestment	Political connections leading to bailing out of some banks and not others. It is misinvestment because the decision was not linked to operational efficiency.
1.1.3.1 Third Order	State Interference	Based on political connections, some banks received support from the government, but not other. The decision was based on affiliations and connection with powerful structure groups.
1.1.3.6	Relationship- Based	Political connections and personal relationships influenced the government's

Third Order		decision which banks to support.
1.1.3.10 Third Order	Administrative Levers of the State	Banks which had strong government support because of personal relationships and maybe access to media received preferential treatment following default of 1998.

#### 41. MFK Renaissance: Baker-Said, (1998g) 1 article

Code	Theme	Notes
1.1 First Order	Management	Appointments
1.1.6 Second Order	Control	A prominent investor was denied an opportunity to stand for the CEO.
1.1.3.10 Third Order	Administrative Levers of the State	Arbitrary application of law, where the candidate was refused the position on a technicality, which it could be argued did not apply in the context of that particular circumstance. Allowing a foreigner to be in charge of an investment vehicle could have made the Russian government vulnerable. Jordan attempted to tackle the dispute by negotiating with the chairman of the Central Bank of Russia.

#### 42. Inkombank: Borisova, (1998c) 1 article

Code	Theme	Notes
1.1 First Order	Management	Board representation.
1.1.6 Second Order	Control	Fight for control.
1.1.6.3 Third Order	General meeting	It appears that Uneximbank-MFK prevented representatives from Inkombank from voting on dismantling the board due to an error on the part of the board. Inkombank representatives did not receive ballots for the vote.

1.1.6.8 Third Order	Third-Party Enforcement	Two banking empires were locked in a battle for control of Severnaya Verf. The courts took a stance and made their decision. It appears that the parties to the conflict were of the same clout and therefore a fairer resolution was more likely.
1.1.6.12 Third Order	Litigation	Inkombank successfully petitioned the St. Petersburg Arbitration Court for an injunction on the meeting. Even though initially the ruling was ignored, the decision of the court was complied with upon the delivery of the documents. The meeting was rescheduled until a later date. Previously, the courts were relied upon when the dispute over the control of a 33 percent stake was being resolved.

#### 43. MOST Bank: (Parallel Coding) Berezanskaya, (1998a) 1 article

Code	Theme	Notes
1.1 1.2 First Order	Management Diversion	Terminated joint venture.
1.1.4 1.2.2 Second Order	Misimplementation Diversion of Claims	Failure to implement a viable joint venture project because the other party was allegedly engaging in serious business misconduct.



1.1.4.5 1.2.2.5 Third Order	Transactions with Self-Interest	MOST Bank terminated a joint venture (United Card Service) with Uneximbank alleging serious misconduct on the part of Uneximbank's officials. The misconduct was likely to have been of benefit to some insiders.
1.1.4.7 1.2.2.7 Third Order	Self-Enforcement	Most-Bank pulled out of the venture citing unwillingness to accept responsibility for the gross misconduct on the part of the joint venture partner.
1.1.4.11 1.2.2.11 Third Order	Shadow of Enforcement	Most-Bank pulled out of the venture citing unwillingness to accept responsibility for the gross misconduct on the part of the joint venture partner. The bank said in a statement that it intended to ask government regulators to investigate the "doubtful actions of a few officials at United Card Service and Uneximbank."

#### 44. Pioneer Group: 'Misdeeds at Bank in Moscow Revealed', (1998) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Unauthorised transactions.
1.2.2 Second Order	Diversion of Claims	Diversions of claims through unauthorised financial transactions.
1.2.2.5 Third Order	Transactions with Self-Interest	Pioneer Group Inc. disclosed unauthorised financial transactions at Pioneer Bank in Moscow which it owned 60 percent of. The asset management company felt it was not in the position to prevent such practice in the future. The unexpectedly high loss for the quarter was attributed to that fact.
1.2.2.7 Third Order	Self-Enforcement	Pioneer group decided to withdraw from the Moscow Banking business altogether following the discovery of unauthorised transactions.

**45. EBRD: Gordeyev, (1998) 1 article**

Code	Theme	Notes
1.1 First Order	Management	Bankruptcy proceedings.
1.1.1 Second Order	Bankruptcy	The EBRD was unable to recover its stake in a bankrupt bank and wrote off its investment.
1.1.1.4 Third Order	Unclear Rules	The put option design under the British law which would have allowed the EBRD and sell back the stake was not recognised by the Russian law (equal treatment of all shareholders) in the face of bankruptcy proceedings.
1.1.1.7 Third Order	Self-Enforcement	The EBRD was unable to recover its stake in a bankrupt bank despite the put option and wrote off its investment.

**46. Tokobank: Bershidsky, (1998a) 1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Failure to enforce a contract.
1.2.2 Second Order	Diversion of Claims	Tokobank used a loophole in the law to avoid settling futures contracts which became highly unprofitable as a result of rouble devaluation.
1.2.2.4 Third Order	Unclear Rules	Tokobank used a loophole in the law to avoid settling futures contracts which became highly unprofitable as a result of the devaluation of rouble.
1.2.2.12 Third Order	Litigation	The court ruled against investors because according to the Russian Civil Code futures contracts were regarded as wagers in the absence of coercion or deceit. Wagers could not be settled by courts.

**47. Rossiisky Kredit: Aliabyev, (1998h) 1 article**

Code	Theme	Notes
1.2 First order	Diversion	Disputed transaction.
1.2.2 Second Order	Diversion of Claims	Refusal to transfer money to a customer
1.2.2.4 Third Order	Unclear Rules	The bank appealed the decision of the court claiming that the client's account had been frozen by tax authorities.
1.2.2.12 Third Order	Litigation	Court ruling was enforced by bailiffs who seized property of the bank.

#### 49. Kosmos TV: Smith, (1998) 1 article

Code	Theme	Notes
1.1 First Order	Management	Dismissal of a director.
1.1.6 Second Order	Control	A renegade director took shareholders to court over his wrongful dismissal. The cable TV station ended up with two headquarters.
1.1.6.4 Third Order	Unclear Rules	The court ruled in favour of the renegade director because it relied on the Labour Code, rather than the Joint Stock Company Law, which was a higher order law and would have protected the shareholders more adequately. The Russian courts, at the time, were much more familiar with the Labour Code than the JSC Law and used the former much more readily. The decision raised concerns since it proved impossible for companies to sack their directors on even legitimate grounds.
1.1.6.6 Third Order	Relationship-Based	Lapshin left after an out-of-court settlement was reached.
1.1.6.12 Third Order	Litigation	Foreign investors and the Russian partners respected decision of the court and reinstated the director.

**50. Channel Five: Whitmore, (1998) 1 article**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.2 First Order	Diversion	Contracting.
1.2.2 Second Order	Diversion of Claims	Diversion of funds through unprofitable advertising contracts and questionable fiscal practices.
1.2.2.5 Third Order	Transactions with Self-Interest	A Finance Ministry audit of St. Petersburg Channel 5 television station revealed a series of unprofitable advertising contracts and questionable fiscal practices that cost the station at least \$7 million in lost revenues over the two year period. The TV channel signed contracts with advertising companies connected to Lisovsky (close ally of Berezovsky). The fees in the contracts were subsequently lowered for no apparent reason and the advertising companies failed to fully repay their debts to the channel.
1.2.2.6 Third Order	Relationship-Based	Personal relationships played an important role at the initial stage of questionable contracting. Lisovsky was allowed to transfer value from Channel 5 to his advertising agencies for the successful re-election campaign. Also, with regard to an unpaid debt of LISS (one of Lisovsky's advertising agencies) to Channel 5, an out of court settlement was reached where only one fourth of the debt was paid despite the case being taken to court.
1.2.2.8 Third Order	Third-Party Enforcement	Third-party enforcement in the form of Berezovsky's support.
1.2.2.10 Third Order	Administrative Levers of the State	Yeltsin's apathy might have been the reward that Lisovsky received for running the successful re-election campaign.
1.2.2.12 Third Order	Litigation	Finance Ministry produced an audit report about financial irregularities to do with advertising contracts. The report led to the

		investigation by the General Prosecutor's Office. Also, the case of non payment by LISS was taken to court.
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## 51. ORT (2 separate disputes)

### 51.1: 'Yeltsin Denies TV Share Trade', (1998) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Transfer of shares.
1.2.2 Second Order	Diversion of Claims	Diversion of claims through non transparent schemes involving leading politicians and businessmen.
1.2.2.5 Third Order	Transactions with Self-Interest	There were alleged transfers of more than one quarter of ORT's shares from Berezovsky to Yeltsin through Korzhakov. Yeltsin's spokesman denied the transaction. Berezovsky, however said that the transfer was ordered by Korzhakov.
1.2.2.6 Third Order	Relationship-Based	This case demonstrates the extent of Berezovsky's proximity to Yeltsin and the government.
1.2.2.10 Third Order	Administrative Levers of the State	The transfer of shares in ORT allegedly took place because Berezovsky wanted to bribe Yeltsin. The presidential administration denied the allegation. Although the actual transaction did take place; high ranking officials kept accusing each other.

### 51.2: Zolotov, (1998) 1 article

Code	Theme	Notes
1.1 First Order	Management	Failure to pay creditors.
1.1.1 Second Order	Bankruptcy	Bankruptcy proceedings following ORT's failure to pay creditors. The government repeatedly stepped in to bail out the company.

1.1.1.8 Third Order	Third-Party Enforcement	The company was protected by the government, not only because it represented an important asset, but perhaps due to the fact the Yeltsin and other high ranking officials allegedly held shares in ORT.
1.1.1.10 Third Order	Administrative Levers of the State	The courts sent marshals to seize the property of ORT following the company's failure to pay the creditors. The government however, extended the credit given to ORT by issuing a presidential decree to that effect.
1.1.1.12 Third Order	Litigation	There were bankruptcy proceedings following ORT's failure to pay creditors. The government repeatedly stepped in to bail out the company. Courts ruled against ORT sending marshals to seize the property in lieu of the debts. The Moscow city bankruptcy committee also filed a case in the Moscow Arbitration Court.

**52. Subway: (Parallel Coding)** Borisova, (1998e); Borisova, & Whitmore, (1998); Schwartz, (1998a); Schwartz, (1998b); Schwartz, (1998d); Schwartz, & Digges, (1998); 'Subway Shop Neglected at St. Pete's Peril', (1998) **7 articles**

Code	Theme	Notes
1.1 1.1 1.2 First Order	Management  Diversion	Joint Venture
1.1.6 1.1.2 1.2.1 Second Order	Control Ownership/ Diversion of Assets	A Russian joint venture partner illegally ousted American partners, renamed the entity, and assumed control and ownership of the business thereby diverting assets and claims.
1.1.6.5 1.1.2.5 1.2.1.5 Third Order	Transactions with Self-Interest	A Russian joint venture partner (Bordug) illegally ousted American partners (East West Invest), renamed the entity, and assumed control and ownership thereby depriving East West Invest of their initial investment for over 2 years.

1.1.6.9 1.1.2.9 1.2.1.9 Third Order	Private Enforcement	<p>When the bailiffs showed up (with all the necessary papers) the management of Minutka did not quietly acquiesce in the process. It was suggested that the Submarine business is quite separate from Minutka.</p> <p>A document dated March 2, 1998, was produced according to which all the assets of Minutka had been transferred to the new corporate entity. An assistant, who identified himself only as Vyacheslav, refused to let a reporter examine the document. Vyacheslav, a thickly built man with close-cropped hair who refused to say what his position in the business was, repeatedly challenged the bailiffs as they tried to fulfil their duties.</p>
1.1.6.10 1.1.2.10 1.2.1.10 Third Order	Administrative Levers of the State	<p>The governor (Vladimir Yakovlev) did not assist the process and used an example of another dispute as a justification for the injustice. However, he (the governor) was under a lot of pressure from foreign community to demonstrate the rule of law and adequate protection. It appears that the local administration was not in the position to solve the case categorically.</p>
1.1.6.12 1.1.2.12 1.2.1.12 Third Order	Litigation	<p>The case of expropriation was taken to the Stockholm International Arbitration Court which ruled in favour of the American partners. Russian Common and Supreme Courts endorsed the decision. However, the bailiffs appointed by the local court struggled to recover the debts. They were not qualified to evaluate the property; their efforts were hindered by the formal change of ownership of Minutka and private security involvement.</p>

**53. Lomonosov Porcelain Factory: Koriukin, (1998b) 1 article**

Code	Theme	Notes
1.1 First Order	Management	Buying stock through brokerages.
1.1.2 Second Order	Ownership/Control	Managers of Lomonosov Porcelain Factory denied foreign investors access to the factory and its books on the grounds that the brokerages that sold the stakes had originally purchased them illegally.
1.1.2.2 Third Order	Inadequate Information	Foreign investors claimed that they had determined that the St. Petersburg brokerages had the right to sell the shares, although they did not know the details of how the brokers had acquired the shares. A financial consultant to the factory, however, said the investors did not exercise due diligence when dealing with the brokerages, which were reported to have been involved in questionable stock transactions in the past. Lomonosov was a closed joint-stock company, which meant a shareholder could not sell his shares to a third-party without other shareholders' approval. The shares were sold through a scheme by which a factory employee gave one of his shares as a gift to an intermediary company, which thus became a shareholder and could buy any number of shares.
1.1.2.5 Third Order	Transactions with Self-Interest	The brokerages picked August for their takeover plan, knowing that the factory had been shut down for a month and a half in June and July and unable to pay its workers. The shares were bought up for half their face value



		of 50 rubles (\$8 at the August exchange rate).
1.1.2.7 Third Order	Self-Enforcement	The factory's management tried to protect themselves from the new investors by denying them access to their property while turning to courts in an effort to reveal illegal practice.
1.1.2.9 Third Order	Private Enforcement	It was alleged that the brokerages were connected with criminal circles which employed practices like physical harassment, (a project manager with Vanguard was brutally beaten with iron rods by unknown men just as he was in the middle of negotiations with KKR and the investment fund managers. St. Petersburg mafia, which profited from the stock deal and was trying to prevent a fair agreement between the factory and foreign investors, was blamed) threats, etc, to persuade employees to sell their stakes cheaply.
1.1.2.12 Third Order	Litigation	Managers of Lomonosov Porcelain Factory denied foreign investors access to the factory and its books on the grounds that the brokerages that sold the stakes had originally purchased them illegally. The factory took the case to a St. Petersburg court which agreed to look into the situation suspecting illegal action.

#### 54. Kuznetsky Mine (Parallel Coding): Rao, (1998e) 1 article

Code	Theme	Notes
1.1 First Order	Management	Stakeholder relations (local authorities).

<p>1.1.2 1.1.4 Second Order</p>	<p>Ownership/ Misimplementation</p>	<p>Local authorities tried to win control from foreign investors over a potentially profitable venture.</p>
<p>1.1.2.1 1.1.4.1 Third Order</p>	<p>State Interference</p>	<p>Local authorities were trying to renationalize assets belonging to a foreign investor – Prosystem GmbH. The plant (Kuznetsky Mine) had a potential; the local administration realised that and decided to get their hands on the property. They started ignoring previous agreements and began legal action against the foreign investor.</p>
<p>1.1.2.4 1.1.4.4 Third Order</p>	<p>Unclear Rules</p>	<p>Kuznetsky was the first Russian mine to be privatized. Prosystem obtained a 40 percent stake in 1991, while another 20 percent went to a Liechtenstein-based company, Tradico. Another 40 percent was held by workers and managers. Some have deemed the privatization unfair given the relatively cheap conditions under which Prosystem bought its stake -\$800,000 and a promise to invest another \$1 million. But Hofer said this was a fair price at the time, given the mine's condition. A Kemerovo arbitration court ruled the privatization of the mine illegal, but an appeals court later invalidated the ruling.</p>

1.1.2.5 1.1.4.5 Third Order	Transactions with Self-Interest	Allegedly, local authorities, attracted by the newly installed modern infrastructure at the mine, attempted to renationalize it. Soon after, a devastating fire broke out in the mine. Moreover, a coal monopoly Rosugol refused to pay its \$2.9m debt despite written pledges.
1.1.2.7 1.1.4.7 Third Order	Self-Enforcement	The Austrian investors (Prosystem GmbH) considered simply leaving the project provided they were reimbursed for their expenses and the 40 percent stake in the mine.
1.1.2.9 1.1.4.9 Third Order	Private Enforcement	Local power structures including administration and federal agencies used a variety of techniques aimed at pressurising foreign investors. There might have been a connection between the events to do with the mine and the fire, beating up of employees, raids of the offices, and murders.
1.1.2.12 1.1.4.12 Third Order	Litigation	The Austrian investor did turn to courts in order to defend the legitimacy of the privatized stake and make a ruling on the outstanding debt.

**55. MCCI (Parallel Coding): Kenyon, (1998c) 1 article**

Code	Theme	Notes
1.1	Management	Lease agreement.

1.2 First Order	Diversion	
1.1.6 1.1.2 1.2.1 Second Order	Control  Ownership/  Diversion of Assets	Russian state-owned entity took control over a viable project from which a foreign investor was forced to withdraw due to concerns over the lease agreement.
1.1.6.1 1.1.2.1 1.2.1.1 Third Order	State Interference	The state company used its influence to renegotiate terms of the lease agreement in its favour. The agreement was previously called into question. An arbitration court in Stockholm, Sweden, ruled that GlavUpDK had reneged on its part of the contract with MCCI by not turning over the lease on the property to the joint venture. Uncertainty drove foreign investors out at which point GlavUpDK continued with the project.
1.1.6.5 1.1.2.5 1.2.1.5 Third Order	Transactions with Self-Interest	The state-owned company (GlavUpDK) used its powers to negotiate the lease agreement in its favour depriving the foreign investor (California-incorporated Moscow Country Club Inc., or MCCI) of any guarantees thus driving the foreign investor out of the project.
1.1.6.10 1.1.2.10 1.2.1.10 Third Order	Administrative Levers of the State	The state-owned company used its power to negotiate the lease agreement in its favour depriving the foreign investor of any guarantees.
1.1.6.12 1.1.2.12 1.2.1.12 Third Order	Litigation	Stockholm arbitration court and a U.S. federal court ruled in favour of the US investor. Without the stamp of a Russian court, the foreign partner could seize foreign assets of the state-owned company (there were insufficient assets to cover the claim), or prove its (GlavUpDK) links with the government and seize the property of the Russian Foreign Ministry.

**56. Standart NMT: Schwartz, (1998c) 1 article**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.2 First Order	Diversion	Increased price of service.
1.2.2 Second Order	Diversion of Claims	The police department was providing security service to a business client and possibly forcing him to pay more money using gangster tactics.
1.2.2.5 Third Order	Transactions with Self-Interest	The police department in St. Petersburg decided to increase the price of security service it offered businesses and forced owners like Igor Rudyenkov of Standart-NMT, (an auto parts store in Kirishi) to pay more.
1.2.2.10 Third Order	Administrative Levers of the State	The police department did not hesitate to enforce its decision (increase the price of security service) by means of such tactics as denying the owner access to the shop, drawing on the economic crimes department to press questionable charges accusing the businessman of selling fake oil (despite the demonstration of the required licences); and traffic police stopping and detaining the businessman for no apparent reason.

**57. Post Office: Solovyova, (1998) 1 article**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.2	Diversion	Non payment to a service provider.

First Order		
1.2.2 Second Order	Diversion of Claims	The Railway refused to carry the mail when the Post Office failed to settle its debt.
1.2.2.5 Third Order	Transactions with Self-Interest	The Post Office was accused of allowing the bureaucrats to pocket revenues and thus forcing the service to accumulate a massive debt. In theory, the Post Office should be a profitable entity because it collects money upfront at rates established by the Communications Ministry well above those necessary to cover its transportation expenses.
1.2.2.7 Third Order	Self-Enforcement	The Railways Ministry decided to stop carriage of post due to non payment. The ministry did not refer to courts. The decision was made at the ministerial level. On the other hand, the stoppage of shipments could be interpreted as a way to win back commercial carriage contracts and bring them under the auspices of the Railways Ministry.

**Appendix 9 b: Templates of Corporate Disputes, 2006**

**1. Aeroflot: Humphries, (2006) 1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Purchasing strategy.
1.2.2 Second Order	Diversion of Claims	Diversion of claims through the purchasing strategy that was not shareholder-centred.
1.2.2.1 Third Order	State Interference	The government had a different agenda in terms of the purchasing strategy which sought to recreate the national industry and build political allies.
1.2.2.10 Third Order	Administrative Levers of the State	Major shareholders are more profit driven, but failed to get anywhere with pushing their case.

**2. Svyazinvest: 'Svyazinvest Sale Delayed', (2006) 1 article**

Code	Theme	Notes
1.1 First Order	Management	Sale of a stake.
1.1.2 Second Order	Ownership	Uncertainty concerning the sale of a 75 percent stake in the company.
1.1.2.2 Third Order	Inadequate Information	The government kept delaying the promised sale of the 75 percent stake in Svyazinvest.
1.1.2.10 Third Order	Administrative Levers of the State	The government broke its promise to sell a 75 percent stake in Svyazinvest to strategic investors because it was looking for a politically acceptable partner.

**4. VimpelCom: Levitov, (2006a) 1 article**

Code	Theme	Notes
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1.1 First Order	Management	Acquisition strategy.
1.1.3 Second Order	Misinvestment	Misinvestment by misleading shareholders at an extraordinary shareholders meeting.
1.1.3.2 Third Order	Inadequate Information	The original decision regarding a controversial purchase of Ukrainian Radiosystems was made at an extraordinary shareholders meeting based on misleading information.
1.1.3.3 Third Order	General Meeting	Both shareholders of VimpelCom have a blocking stake. One of them was interested in a purchase of a competitor of the other. The Russian shareholder provided misleading information at the disputed extra-ordinary shareholders meeting and got the vote its way.
1.1.3.11 Third Order	Shadow of Enforcement	Telenor threatened to take the case to an American court.
1.1.3.12 Third Order	Litigation	Telenor disputed the decision in Russian courts.

**5. MagaFon: (Parallel Coding) Belton & Levitov, (2006a); Belton & Levitov, (2006b) 2 articles**

Code	Theme	Notes
1.2	Diversion	Minister as ultimate beneficiary.
1.1 First Order	Management	
1.2.2 1.1.2 Second Order	Diversion of Claims Ownership	Diversions of claims through dilution by a government minister who denied his status as the ultimate beneficiary.



1.2.2.2 1.1.2.2 Third Order	Inadequate Information	IT and Communications Ministry spokesman denied that Reiman was among the fund's owners. It has been claimed that 'Reiman was neither a beneficiary nor a shareholder of the companies described'. However, the Zurich court found that Reiman was the ultimate beneficial owner of IPOC.
1.2.2.5 1.1.2.5 Third Order	Transactions with Self-Interest	The minister diluted the states interest in MegaFon using his powers as the IT and Communications Minister.
1.2.2.10 1.1.2.10 Third Order	Administrative Levers of the State	The minister diluted the state's interest in MegaFon using his powers as the IT and Communications Minister.
1.2.2.12 1.1.2.12 Third Order	Litigation	The Zurich arbitration tribunal ruled that the IT and Communications Minister Leonid Reiman was the ultimate beneficiary of the IPOC fund.

**6. AvtoVaz: (Parallel Coding) 'AvtoVAZ Investigation Closed', (2006);**

Smolchenko, (2006b) **2 articles**

Code	Theme	Notes
1.1 First Order	Diversion	Government seeking greater control.

1.1.6 1.1.5 Second Order	Control Taxes	The government was seeking to re-establish control over the car manufacturer by opening and closing criminal investigations (including probes into the non-payment of taxes) and bringing in a symbolic suit against the joint venture partner GM.
1.1.6.1 1.1.5.1 Third Order	State Interference	The government was seeking to re-establish control over the car manufacturer by opening and closing criminal investigations and bringing in a symbolic suit against GM, the joint venture partner.
1.1.6.4 1.1.5.4 Third Order	Unclear Rules	The Russian Court system bounced the criminal charges from court to court, but eventually returned the cases to the prosecutor's office which decided to cancel the investigation. No explanation was given as to why.
1.1.6.10 1.1.5.10 Third Order	Administrative Levers of the State	The Russian government's technique was based on intimidating power groups within AvtoVaz with overly serious (in this case probably not unfounded) and symbolic charges. Subsequently, the charges were dropped because the influential parties agreed to co-operate with the government. The suit against the joint venture was used in order to redress the balance between the joint venture partners in favour of the Russian side.
1.1.6.12 1.1.5.12 Third Order	Litigation	The Russian Court system bounced the criminal charges from court to court, but eventually returned the cases to the prosecutor's office which decided to cancel the investigation. No explanation was given as to why. Also, the government friendly management sued its joint venture partner GM for a symbolic sum of \$60.

## 10. Rosneft (5 separate disputes)

### 10.1: Belton, (2006m); 'Rosneft Consolidates Yugansk Stake', (2006) 2 articles

Code	Theme	Notes
1.2 First Order	Diversion	Asset transfers.
1.2.2 Second Order	Diversion of Claims	Diversions of shares through a non transparent company.
1.2.2.2 Third Order	Inadequate Information	An unknown (possibly shell) firm, Baikal Finance Group, received assets of Yukos, held on to them and later transferred those to Rosneft. A similar scheme used Rosneftgaz as an intermediary. The schemes lacked transparency and it is possible that a substantial amount of money changed hands.
1.2.2.5 Third Order	Transactions with Self-Interest	Officials acting in their self-interest devised these non-transparent schemes because of which (possibly) a substantial amount of money changed hands.
1.2.2.10 Third Order	Administrative Levers of the State	Officials acting in their self-interest devised a scheme whereby the company's assets were transferred by means of non transparent schemes. One of the schemes also protected Rosneft from legal risks arising from the much disputed auction of Yugansk.

### 10.2: Belton, (2006r); Belton, (2006s); Humber, (2006h) 3 articles

Code	Theme	Notes
1.2 First Order	Diversion	Consolidation.
1.2.2 Second Order	Diversion of Claims	Undervaluation of shareholders' stakes in Rosneft subsidiaries.

1.2.2.5 Third Order	Transactions with Self-Interest	Some minority shareholders felt that the terms of consolidation were ten times below what they should have been. An analyst however suggested that the price of the subsidiary's shares was inflated by speculative purchases from investors who counted on better consolidation terms ahead of the IPO.
1.2.2.4 Third Order	Unclear Rules	It is difficult to see how the minority can protect its interests since by law the company is allowed to pick a method of valuation. Clearly, management would use the most favourable one and with the legal profession lacking expertise, accountants have a greater freedom when it comes to 'massaging' the figures.
1.2.2.11 Third Order	Shadow of Enforcement	Minority shareholders threatened to sue Rosneft.
1.2.2.12 Third Order	Litigation	The fund's director felt that the interests of minority were trampled with and filed a complaint with a regional court.

### 10.3: (Parallel Coding) Belton, (2006s) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Parent - Subsidiary
1.2.2 1.2.1 Second Order	Diversion of Claims Diversion of Assets	Transfer pricing and asset stripping of the subsidiaries.
1.2.2.5 1.2.1.5 Third Order	Transactions with Self-Interest	Alleged asset stripping and transfer pricing took place at Rosneft's subsidiaries. The subsidiaries complained to the government.
1.2.2.10 1.2.1.10 Third Order	Administrative Levers of the State	Rosneft acknowledged transfer pricing and asset stripping saying that the former was common practice within oil industry and the latter was the result of Rosneft's major investment in the subsidiary.

**10.4: 'Protests Grow Over Barinov's Arrest', (2006) 1 article**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.1 First Order	Management	Stakeholder management.
1.1.5 Second Order	Taxes	Alleged non-payment of taxes by a Rosneft's subsidiary.
1.1.5.1 Third Order	State Interference	The government detained Barinov on suspicion of fraud and embezzlement allegedly after/because he campaigned against Rosneft's subsidiary which did not pay taxes and broke ecological standards. Rosneft's spokesman said that the company was acting in accordance with all signed agreements and had nothing to do with the detention of the governor.

1.1.5.10 Third Order	Administrative Levers of the State	It is possible that Rosneft relied on administrative support and ordered formal institutions to detain Barinov. From the report it is impossible to determine whether Barinov was actually guilty. It is however clear that the state and state companies would not hesitate to revive charges against their opponents (both political and economic) and use those to protect their interest.
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**10.5: (Parallel Coding)** Belton, (2006k); Belton, (2006l); Belton, (2006m); Belton, (2006n); Belton, (2006r); 'Rosneft to Sell More IPO Shares in Russia', (2006) **6 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Legitimacy
1.2.2  1.2.1 Second Order	Diversion of Claims  Diversion of Assets	Legitimation of Rosneft's acquisition of Yukos' assets.
1.2.2.5 1.2.1.5 Third Order	Transactions with Self-Interest	The government and Rosneft's officials used IPO in London as an instrument for legitimising the status of the acquired assets (previously belonging to Yukos).
1.2.2.6 1.2.1.6 Third Order	Relationship-Based	Foreign companies like BP and Petronas were keen to support Rosneft's IPO in order to please the Russian government. The government made it clear that such support will be critical when it comes to decisions to do with licensing and access to resources.
1.2.2.10 1.2.1.10 Third Order	Administrative Levers of the State	The IPO in London and the fact that Rosneft was fully backed by the government meant that it was immune from the rulings of foreign courts.
1.2.2.12 1.2.1.12 Third Order	Litigation	Although the company was being sued in various locations by minority shareholders, the rulings of international courts had to be upheld by a Russian court in order to compel Rosneft

		to pay.
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## 11. Gazprom (5 separate disputes)

### 11.1: Korchagina, (2006d) 1 article

Code	Theme	Notes
1.1 First Order	Management	Previous agreements.
1.1.2 Second Order	Ownership	Ownership of a 40 percent stake in a gas field is disputed.
1.1.2.1 Third Order	State Interference	An agreement that a significant ownership stake would go to Moncrief was broken probably because BASF received a much stronger political support.
1.1.2.4 Third Order	Unclear Rules	An agreement was not honoured by Gazprom possibly because the government found a more acceptable (politically) partner to develop the field.
1.1.2.10 Third Order	Administrative Levers of the State	The initial agreement specified that all disputes should be settled in Russian courts hence it was probably possible for Gazprom to disregard the agreement completely.
1.1.2.12 Third Order	Litigation	The initial agreement specified that all disputes should be settled in Russian courts hence it was probably possible for Gazprom to disregard it completely.

### 11.2: (Parallel Coding) Belton, (2006h) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Transfer of assets.
1.2.1	Diversion of Assets Diversion of	Diversion of assets and claims from Gazprom to Itera through crony deals valued at as much as \$4 billion a year and then back to Gazprom

1.2.2 Second Order	Claims	through a politically backed consolidation.
1.2.1.5 1.2.2.5 Third Order	Transactions with Self-Interest	Backed by Putin's administration, the state company Gazprom transferred assets from the largest independent gas producer Itera in order to redress the balance in its favour. Previously Itera siphoned off a great deal of Gazprom's assets by means of crony deals.
1.2.1.10 1.2.2.10 Third Order	Administrative Levers of the State	The former managers of Gazprom were replaced by those completely loyal to Putin. Hence, Putin's administration made it possible for Gazprom to regain some of the key assets that had been previously transferred to Itera.

**11.3: (Parallel Coding) Belton, (2006i); Elder, (2006e); Kim, (2006b); Zhdannikov, (2006a) 4 articles**

Code	Theme	Notes
1.2 1.1 First Order	Diversion Management	Competition.
1.2.1 1.1.2 Second Order	Diversion of Assets Ownership	Diversion of assets in favour of Gazprom by means of threats to revoke licenses from major companies using environmental allegations as an excuse.
1.2.1.1 1.1.2.1 Third Order	State Interference	Threats by the Natural Resources Ministry to revoke operating licenses from Shell and TNK-BP have been interpreted as a means of putting government pressure on foreign oil majors to accept Gazprom's entry into their projects.
1.2.1.4 1.1.2.4 Third Order	Unclear Rules	The government decided to consolidate control over the oil and gas sector (Gazprom was the main beneficiary of such action), yet delayed the law on strategic assets.
1.2.1.10 1.1.2.10	Administrative Levers of the State	The government and Gazprom put pressure on foreign led projects using environmental non-compliance as a negotiating tool in order to secure favourable terms for Gazprom's (or



Third Order		Rosneft) entry.
1.2.1.12 1.1.2.12 Third Order	Litigation	The development of the law on strategic assets which would have clarified the legal side of things in these sorts of disputes was delayed several times.

#### 11.4: Elder, (2006c) 1 article

Code	Theme	Notes
1.1 First Order	Management	Appointments
1.1.6 Second Order	Control	A Gazprom official accumulated too much power and, allegedly, because of that was replaced by a Putin's loyalist.
1.1.6.10 Third Order	Administrative Levers of the State	It has been suggested that Ryazanov became so powerful that perhaps started to represent a threat to some other high ranking officials within Gazprom and the government. Ryazanov was replaced with an ex KGB agent from St. Petersburg who worked at the mayor's office at the same time as Putin.

#### 11.5: (Parallel Coding) Belton, (2006g); Belton, (2006j); Boykewich, (2006a); 'Ukraine Deal Answers Only One Question', (2006) 4 articles

Code	Theme	Notes
1.2 1.1 First Order	Diversion Management	Contracts.
1.2.2 1.1.2	Diversion of Claims/ Ownership	Gazprom cut supplies to Ukraine and Belarus in order to renegotiate terms of the existing contracts and arrangements. The

Second Order		new agreement features a middle man with an un- disclosed ownership structure.
1.2.2.1 1.1.2.1 Third Order	State Interference	Despite the formal agreement between Russia, Ukraine and Belarus, Gazprom cut supplies in order to increase the price of gas and extend its grip over the export pipeline to Europe. Gazprom and the Russian government felt that they were not getting a good deal and perhaps argued legitimacy of their actions in those terms.
1.2.2.2 1.1.2.2 Third Order	Inadequate Information	In the instance of the agreement with Ukraine, a company with an undisclosed ownership structure (Rosukrenergo) was nominated as a trader. As a result of that, billions of dollars went unaccounted for.
1.2.2.4 1.1.2.4 Third Order	Unclear rules	Gazprom suddenly moved to breach a five-year contract signed with Ukraine in August 2004 that set the gas price at \$50.
1.2.2.5 1.1.2.5 Third Order	Transactions with Self-Interest	There was a vast disparity in the two sides' assessment of Beltransgas' worth: Belarus put it at \$5 billion, while Gazprom's assessment of it was a mere \$600,000 <sup>173</sup> . Additionally, because of the undisclosed ownership structure of Rosukrenergo, billions of dollars went unaccounted for.
1.2.2.9 1.1.2.9 Third Order	Private Enforcement	The gas export agreement between Russia and Ukraine involved a middleman (RosUkrEnergo) with a murky ownership structure. Some suggested it was linked to the criminal underworld. The company's auditor KPMG resigned because of its concerns over possible damage to reputation.
1.2.2.10 1.1.2.10 Third Order	Administrative Levers of the State	Gazprom cut gas supplies breaking existing contracts and agreements. The company used its monopoly power to renegotiate the terms of the contracts. In the instance of the

<sup>173</sup> Clearly the Belarusian side was playing the political card. It is probably understood that Gazprom would pay a premium on the company's assets for the sake of extending its monopoly powers. The question is how much Gazprom would be willing to part with.

		agreement with Ukraine, a company with an undisclosed ownership structure (Rosukrenergo), but possibly connected to the government, was nominated as a trader.
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## 12. Yukos (7 separate disputes)

**1. (Parallel Coding):** Abdullaev, (2006); Belton, (2006a); Belton, (2006b); Belton, (2006f); Belton, (2006o); Belton, (2006q); Belton, (2006s); Belton, (2006x); Belton, (2006y); Boykewich, (2006b); 'Date Set for Yukos Case, Shares Plunge', (2006); 'Gazprombank Tapped in Yukos Sell-Off', (2006); Korchagina, (2006a); Korchagina, (2006f); 'Lawyer's Jail Time Cut to 6 1/2 Years', (2006); Mauldin, (2006b); Medetsky, (2006a); Medetsky, (2006c); Schreck, (2006); Smolchenko, (2006c); 'These Signals Are Less Than Transparent ', (2006); 'Yukos Exec Could Get 9 Years', (2006); 'Yukos Pegs Hopes on Lower Debt, More Oil', (2006)      **23 articles**

Code	Theme	Notes
1.1 First Order	Management	Re-nationalization, stakeholder management.
1.1.2 1.1.6 1.1.5 Second Order	Ownership/ Control Taxes	Re-nationalization of the company through questionable tax allegations.
1.1.2.1 1.1.6.1 1.1.5.1 Third Order	State Interference	The government, possibly arbitrary, imposed back tax bills on the company in an effort to seize control over its main assets. The decision was likely to be linked to Khodorkovsky's support of political opposition.
1.1.2.5 1.1.6.5 1.1.5.5 Third Order	Transactions with Self-Interest	A Moscow court sanctioned the arrest of Yukos' executive vice president, a day after he was charged with embezzlement and money laundering. Aleksanyan was detained by the Prosecutor General's Office just days after his appointment as Yukos vice president. He was charged with stealing 8 billion rubles (\$290.3 million) in property and 3.6 billion rubles in shares belonging to companies tied to Eastern Oil Company. This case was part of the government's onslaught

		on Yukos.
1.1.2.9 1.1.6.9 1.1.5.9 Third Order	Private Enforcement	Campaign of intimidation in the form of beating, jailing etc. was used in order to silence Khodorkovsky's Russian lawyers. International lawyers were refused visas or expelled from the country.
1.1.2.10 1.1.6.10 1.1.5.10 Third Order	Administrative Levers of the State	The government used tax authorities in order to seize control of Yukos. Khodorkovsky was sentenced on fraud and tax evasion charges. International lawyers were refused visas or expelled from the country. The prosecutor's office and tax authorities were instrumental in the enforcement of the government's objectives. It has been alleged that a state-owned company such as Gazprom or Rosneft could buy a controlling stake in Yukos for \$3 billion to \$4 billion and then use their leverage to lift its tax debts.
1.1.2.12 1.1.6.12 1.1.5.12 Third Order	Litigation	The case was disputed in local and international courts including the US court case when high profile government officials were 'legally served'. The government's onslaught was eventually legitimised by the international community when a British judge cleared the way for Rosneft's listing on the LSE.

**12.2: Belton, (2006b); Belton, (2006f) 2 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Questionable transactions.
1.2.2	Diversion of Claims	There were numerous accusations of money laundering on the part of former Yukos

Second Order		executives.
1.2.2.5 Third Order	Transactions with Self-Interest	It has been alleged that Golubovich had conducted transactions worth hundreds of millions of dollars every year through various firms between 1996 and 2000. It has been claimed that Golubovich had forged signatures in several asset transactions. Moreover, the Prosecutor General's Office accused Theede and Osborne of siphoning off more than \$10 billion of assets out of Yukos into foreign holdings. Former Yukos CFO Bruce Misamore and Yukos lawyer David Godfrey, the managers of a Dutch-based Yukos subsidiary, were also under investigation. Aleksanyan was detained by the Prosecutor General's Office just days after his appointment as Yukos vice president. He was charged with stealing 8 billion rubles (\$290.3 million) in property and 3.6 billion rubles in shares belonging to companies tied to Eastern Oil Company.
1.2.2.2.6 Third Order	Relationship-Based	Former Federal Security Service General Andrei Lych co-ran Rusскиye Produkty, which is a major supplier of coffee, tea and other foodstuffs. Former colleagues of Golubovich's have suggested that his connections with a former high-ranking Federal Security Service (FSB) officer might have staved off arrest attempts against him.
1.2.2.9 Third Order	Private Enforcement	The Kremlin was seeking former Khodorkovsky partner Leonid Nevzlin's extradition from Israel on charges that he had ordered a string of murders and attempted murder. Nevzlin denies the charges. Also, the Russian prosecutors

		drafted a request for Golubovich's extradition on charges of participating in an "organized criminal group" that committed large-scale fraud <sup>174</sup> . Golubovich in turn, claimed that two unsuccessful attacks on his family appeared to be "acts of intimidation" aimed at scaring him out of Russia as the legal attack against Yukos mounted in 2003. Also cases involving Aleksanyan, Bakhmina and other Khodorkovsky's former colleagues cannot be disregarded as unconnected to private enforcement.
1.2.2.12 Third Order	Legislation	The government put significant pressure on courts and other formal institutions in order to make sure that those act in line with the politically imposed will and with the required level of efficiency. E.g. Luxembourg-based Yukos Capital sued (Moscow Arbitration Court) its bankrupt parent company Yukos for \$4.8 billion in debts, which could make it the third-largest creditor. It has been suggested that Yukos Capital could win the case only if it had an agreement with Gazprom to sell the debt once the court rules in its favour.

### 12.3: Mauldin, (2006b) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Inside information.
1.2.2 Second Order	Diversion of Claims	It has been alleged that Gazprombank executives used inside information when they sold Yukos shares short one day before a Russian court upheld a back tax bill of \$3.5 billion against the company. Gazprombank may have profited by as much as \$500,000.

<sup>174</sup> Former colleagues said they feared Russian law enforcement agencies were trying to trap Golubovich into testifying against his partners in return for a light sentence as the Kremlin prepared to finish off its assault on Khodorkovsky and his Menatep empire.

1.2.2.4 Third Order	Unclear Rules	Insider trading was not a crime under the Russian law at the time, but the markets service were preparing legislation that would criminalize such trades.
1.2.2.5 Third Order	Transactions with Self-Interest	A lawyer representing U.S. shareholders of Yukos claimed that Gazprombank executives used inside information when they sold Yukos shares short one day before a Russian court upheld a back tax bill of \$3.5 billion against the company. Gazprombank may have profited by as much as \$500,000.
1.2.2.10 Third Order	Administrative Levers of the State	It is entirely possible that Gazprom officials relied on insider information when they sold Yukos shares one day before a court decision.
1.2.2.12 Third Order	Litigation	A lawyer representing U.S. shareholders of Yukos claimed that Gazprombank executives used inside information when they sold Yukos shares short one day before a Russian court upheld a back tax bill of \$3.5 billion against the company.

**12.4:** Belton, (2006c); Belton, (2006u); Belton, (2006w); Belton, (2006x); 'Date Set for Yukos Case, Shares Plunge', (2006); 'Gazprombank Tapped in Yukos Sell-Off', (2006); Schreck, (2006); Skarzinskaite (2006) **8 articles**

Code	Theme	Notes
1.1 First Order	Management	Sale of assets.
1.1.1 Second Order	Bankruptcy	Politically motivated bankruptcy proceedings.
1.1.1.1 Third Order	State Interference	In order to make sure that Yukos did not find a way to avoid bankruptcy, the government initiated a set of new charges (may be legitimate) and used the Prosecutor General's Office and the Russian courts to prevent the sale of the Mazeikiu refinery.
1.1.1.2 Third Order	Inadequate Information	The biggest problem was a lack of information in the West about Yukos and GML assets, which, according to different

		estimates, totalled between \$5 billion and \$20 billion.
1.1.1.5 Third Order	Transaction with Self-Interest	<p>There were new money laundering charges brought against Khadarkovsky and Lebedev as part of a centralised effort to dismantle Yukos. All of the allegations refer to value reducing schemes set up in the 90s early 00s.</p> <p>These allegations could be interpreted as a way (for the Russian government) not to compensate foreign shareholders for the residual value of the company.</p>
1.1.1.10 Third Order	Administrative Levers of the State	In order to make sure that Yukos did not find a way to avoid bankruptcy, the government initiated a set of new charges (may be legitimate) and used the Prosecutor General's Office and the Russian courts to prevent the sale of the Mazeikiu refinery.
1.1.1.12 Third Order	Litigation	Eventually, the rulings were supported by a US court. Initially, Yukos International UK refused to comply with the rulings of the Russian court. But when the US court made its ruling, the international unit accepted it.

**12.5: 'Rebgun Fires Yukos Dutch Unit Chiefs', (2006) 1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Appointments.
1.2.1 Second Order	Diversion of Assets	Hiding assets using a complex web of transactions.



1.2.1.3 Third Order	General Meeting	A shareholder meeting which was acknowledged by a Dutch court as legitimate authorised the decision of the Yukos receiver to fire managers accused of hiding assets in a complex web of transaction.
1.2.1.7 Third Order	Self-Enforcement	The decision to get rid of the two Yukos managers was made by the court appointed Yukos receiver and enforced by means of an extraordinary shareholder meeting that was ruled to be legitimate by a Dutch court. The two managers were accused of trying to hide the company's assets.
1.2.1.12 Third Order	Litigation	The decision to get rid of the two Yukos managers was made by the court appointed Yukos receiver and enforced by means of an extraordinary shareholder meeting that was ruled to be legitimate by a Dutch court. The two managers were accused of trying to hide the company's assets.

**12.6:** Belton, (2006c); Belton, (2006d); Belton, (2006v); Belton, (2006x); Belton, (2006y); Korchagina, (2006b) **6 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Valuation.
1.2.1 Second Order	Diversion of Assets	Undervalued assets to the benefit of Rosneft.
1.2.1.5 Third Order	Transactions with Self-Interest	Valuations of Yukos assets were carried out in such a way as to suit Rosneft. A number of alternative (more independent), valuations including that by UBS, produced substantially higher figures.

1.2.1.10 Third Order	Administrative Levers of the State	The state dictated the terms of valuations. Even though Yukos managers asked for alternative valuations, they were completely disregarded. It is probable that reputable audit firms did not want to protest too loudly because if they did, they risked getting on the wrong side of the Russian government.
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**12.7: Belton, (2006w); Belton, (2006x) 2 articles**

Code	Theme	Notes
1.1 First Order	Management	Appointment.
1.1.6 Second Order	Control	A subordinate refused to follow the orders of the superior who represented the interests of the sole shareholder in the unit. Instead of the proposed appointment, the person who was fired got promotion.
1.1.6.5 Third Order	Transactions with Self-Interest	Allegedly, there were discounted sales to unnamed third parties from the Yukos' Trading House leading to a short fall of between \$50m. and \$100m.
1.1.6.7 Third Order	Relationship-Based	Mr. Nazarov managed to get promoted because of the compromise that he had reached with the government.
1.1.6.10 Third Order	Administrative Levers of the State	It is unlikely that such an act of insubordination could have been possible without the pre agreed support of the government and/or high ranking officials from Rosneft. Clearly the government used its administrative resource to deflect Mr Nazarov to their side. <sup>175</sup>

**13. Shell (Parallel Coding):** '\$10Bln Behind Oil Difficulties', (2006); Elder, (2006a); Elder, (2006b); Elder, (2006d); Elder, (2006f); Elder, (2006g); Elder, (2006h); Elder, (2006i); Elder, (2006j); Elder, (2006k); Elder, (2006l); Elder, (2006m); Elder, (2006n); Elder,

<sup>175</sup> There were more instances that could have been included in the coding. Those can be found in the explanatory notes and code summaries.

(2006q); 'Hurting the Future of Energy Deals', (2006); Kim, (2006a); Korchagina, (2006e); Miles, (2006); 'Mitvol Takes His Crusade to Sakhalin', (2006); Putin Hopes for Sakhalin-2 Deal With Shell', (2006); 'Shell Says Pressure May Delay Project', (2006); 'Shell, Exxon Under Fire on Sakhalin', (2006); Zhdannikov, (2006b) ; Zhdannikov, (2006c); Zhdannikov, & Miles, (2006) **25 articles**

Code	Theme	Notes
1.1 1.2 First Order	Management Diversion	Renegotiation of contractual terms, competition, stakeholder management.
1.1.4 1.1.2 1.2.1 Second Order	Misimplementation Ownership Diversion of Assets	Renegotiation of the ownership structure - Shell was forced to accept new terms or face serious environmental allegations.
1.1.4.1 1.1.2.1 1.2.1.1 Third Order	State Interference	The government helped Gazprom enter the Sakhalin 2 project by accusing Shell of environmental violations. The environmental allegations were used as a bargaining tool to ensure favourable terms of Gazprom's entry. Shell's investment was protected by the PSA which required consent from all parties to the contract before any changes were made. Eventually, Shell gave up when they realised that it was impossible to fight the allegations in the Russian courts which were under strict instructions to make rulings consistent with the government's agenda. The Natural Resources Ministry with its powers to revoke licenses was used as a key instrument in the negotiation process.
1.1.4.10 1.1.2.10 1.2.1.10 Third Order	Administrative Levers	The government used the Natural Resources Ministry and a number of mid ranking officials in order to force Sakhalin Energy accept Gazprom's entry on favourable terms. Previously, the Russian government was angered by Shell when the company increased its cost estimate of the project. Under the PSA agreement, that would have meant that the government would have to wait longer before it received any money from the project. Because of the new cost estimate and high price of oil and gas, the

		government decided to renegotiate terms of the contract which admittedly were not in Russia's best interests.
1.1.4.11 1.1.2.11 1.2.1.11 Third Order	Shadow of Enforcement	Selective application of law becomes visible in the context of Gazprom's desire to enter the project. The threat of license withdrawal based on environmental violations subsided/evaporated once Gazprom pushed/bullied its way into the project as a majority shareholder.
1.1.4.12 1.1.2.12 1.2.1.12 Third Order	Litigation	The government used the Natural Resources Ministry and a number of mid ranking officials in order to force Sakhalin Energy accept Gazprom's entry in to the Sakhalin project on favourable terms. The Natural Resources Ministry withdrew a number of operational licenses further to purported environmental violations <sup>176</sup> . The Ministry was also prepared to argue the case in an international arbitration court in Stockholm. Also, some consideration was given to the terms of the PSA. Finally, strategic reciprocity was featured in the government rhetoric.

**14. Total: (Parallel Coding) Clark & Humber, (2006); Elder & Wall, (2006) 2 articles**

Code	Theme	Notes
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<sup>176</sup> It is extremely difficult not to violate environmental rules in the process of oil and gas extraction, particularly if you are forced to use subcontractors which you have little control over. Clearly, based on the technical point of law, the government had the right to revoke licenses and some violations probably did take place (this made it possible for the government to attack the PSA which offered a great deal of protection to foreign partners). However, selective application of law becomes visible in the context of Gazprom's desire to enter the project.

1.1 1.2 First Order	Management Diversion	Competition, managing stakeholder, renegotiating contracts.
1.1.2 1.2.2 Second Order	Control Diversion of Claims	The government was seeking to re-establish control over the country's oil and gas industry. The government used reviews by the subsoil resource agency (acting on its behalf) in order to force international companies like Total to renegotiate terms of the PSA agreements.
1.1.2.1 1.2.2.1 Third Order	State Interference	The Russian government used its usual tactics of bullying foreign companies into compliance (approve amendments to the PSA) by bringing allegations against oil majors. In the instance of Total it was the subsoil resources agency that blamed Total for breaking the license terms (inflating costs and producing too little oil).
1.1.2.10 1.2.2.10 Third Order	Administrative Levers of the State	Total, on the other hand, had the protection offered by the PSA agreement which stipulated the necessity of bilateral consent if amendments to the existing terms were to be made. The government clearly had an edge over the legal protection at the disposal of Total.
1.1.2.12 1.2.2.12 Third Order	Litigation	The Russian government felt it was not in the interests of the country to allow foreign led projects to continue to operate under the original PSA terms. The decision was based on the fact that macro economic conditions i.e. sharp increases in oil prices rendered the PSA agreements highly unprofitable for the Russian side. The decision to re-establish the ownership structure came from the government and was contrary to the agreements and promises made in the past.

**15. ExxonMobil: Elder & Wall, (2006); Elder, (2006i) 2 articles**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.1 First Order	Management	Competition, managing stakeholder, renegotiating contracts.
1.1.6 Second Order	Control	The government was seeking to re-establish control over the country's oil and gas industry. The government used the Federal Service for Ecological, Technological and Atomic Inspection to force international companies like ExxonMobil to renegotiate terms of the PSA agreements.
1.1.6.1 Third Order	State Interference	The Russian government felt it was not in the interests of the country to allow foreign led projects to continue to operate under the original PSA terms. The decision was based on the fact that macro economic conditions i.e. sharp increases in oil prices rendered the PSA agreements highly unprofitable for the Russian side. The decision to re-establish the balance comes from the government and in all probability was contrary to the agreements and promises made in the past.
1.1.6.10 Third Order	Administrative Levers of the State	The Russian government used its usual tactics of bullying foreign companies into compliance by bringing allegations against oil majors. In the instance of ExxonMobil it was the Federal Service for Ecological, Technological and Atomic Inspection that blamed ExxonMobil for violations in the area of industrial and environmental safety.

## 16. TNK-BP (2 separate disputes)

**16.1:** Belton, (2006e); Belton, (2006t); Belton, (2006p); Elder, (2006o); Elder, (2006h); Elder, (2006q); Elder, & Korchagina, (2006); Kim, (2006b); Medetsky, (2006b); Miles, (2006); Simpson, (2006); 'These Signals Are Less Than Transparent', (2006); Zhdannikov, (2006a); 'Trutnev Agrees to TNK-BP Well Plan', (2006); Levitov, & Elder, (2006)

### 15 articles

Code	Theme	Notes
1.1 1.2 First Order	Management Diversion of Claims	Competition, managing stakeholder, renegotiating contracts.
1.1.6 1.1.2 1.2.1 Second Order	Control Ownership/ Diversion of Assets	The government used environmental violations and non-compliance with the license agreement to force TNK-BP to accept 'Gazprom tailored' terms of restructuring.
1.1.6.1 1.1.2.1 1.2.1.1 Third Order	State Interference	There was formal non-compliance with the license terms because Gazprom denied TNK-BP access to the export pipeline on the grounds of its monopoly status. TNK-BP were required to produce more gas for the local market which did not exist. The government felt it was necessary to renegotiate the terms of oil and gas contracts

		relating to major foreign led projects.
1.1.6.6 1.1.2.6 1.2.1.6 Third Order	Relationship-Based	TNK-BP agreed to form a joint venture with Gazprom as it sought better government relations amid a crackdown on foreign energy companies. Criminal allegations of purported license violations were used to force TNK-BP to co-operate with Gazprom. TNK-BP agreed to invite Gazprom into its projects and by doing so, probably did not lose as much as others. Moreover, BP participated in Rosneft's IPO in London as a relationship building exercise with the Russian government.
1.1.6.9 1.1.2.9 1.2.1.9 Third Order	Private Enforcement	It is possible that the murder of the TNK-BP official was a contract hit connected to the company's operations in the country. It is unlikely to have been ordered by the federal government and probably was planned on the local level.
1.1.6.10 1.1.2.10 1.2.1.10 Third Order	Administrative Levers of the State	The government used the Prosecutor General's Office and the Ministry for Natural Resources in order to pressurise the company into acceptance of the restructuring plan which involved Gazprom's participation. The preference of this solution lies in the fact that companies in this industry inevitably violate environmental law and license agreements.
1.1.6.11 1.1.2.11 1.2.1.11 Third Order	Shadow of Enforcement	The government used environmental violations and non-compliance with the license agreement to force TNK-BP to accept 'Gazprom tailored' terms of restructuring <sup>177</sup> . The mounting campaign against foreign oil projects prompted warnings from foreign diplomats and analysts that Moscow must clarify its intentions if it

<sup>177</sup> Similar pressure was faced by Total, ExxonMobil, LUKoil and Yukos.



		hopes to continue attracting foreign investment.
1.1.6.12 1.1.2.12 1.2.1.12 Third Order	Litigation	The government used the Prosecutor General's Office and the Ministry for Natural Resources in order to pressurise the company into acceptance of the restructuring plan which involved Gazprom's participation. There was formal non-compliance with the license terms because Gazprom denied access to the export pipeline on the grounds of its monopoly status <sup>178</sup> . TNK-BP were required to produce more gas for the local market which did not exist. In addition, the prosecutor general's office opened an investigation into TNK-BP for acquiring state secrets from top government officials <sup>179</sup> .

## 16.2: Elder, (2006p) 1 article

Code	Theme	Notes
1.1 First Order	Management	Managing stakeholders
1.1.5 Second Order	Taxes	Undisputed back taxes.

<sup>178</sup> The preference of this solution lies in the fact that companies in this industry inevitably violate environmental law and license agreements to some degree, particularly if compliance is made impossible.

<sup>179</sup> The investigation came at a time when the government sought to increase pressure on the oil operator in order to negotiate better terms for Gazprom's entry.

1.1.5.1 Third Order	State Interference	Allegations of unpaid taxes came at a time when the government increased pressure on oil companies in Russia in order to ensure favourable terms for Gazprom's entry into a number of major oil projects as a majority shareholder.
1.1.5.6 Third Order	Relationship-Based	TNK-BP probably learnt from the Yukos experience and did not want to challenge the back taxes claim too aggressively in courts. The fact that the company did pay back taxes may have been viewed as another relationship building opportunity with the Russian government.
1.1.5.10 Third Order	Administrative Levers of the State	TNK-BP agreed to pay the back taxes charges which were by many seen as related to the company's vows.
1.1.5.12 Third Order	Litigation	TNK-BP probably learnt from the Yukos' experience and did not challenge the back taxes claim too aggressively in courts. Interestingly, because the claims related to the pre merger period, it was the Russian shareholders who paid the money.

## 17. LUKoil (2 separate disputes)

### 17.1: Elder, & Wall, (2006); Elder, (2006i) 2 articles

Code	Theme	Notes
1.1 First Order	Management	Competition, managing stakeholder, renegotiating contracts.
1.1.2 Second Order	Ownership	The government was seeking to re-establish control over the country's oil and gas industry.
1.1.2.1 Third Order	State Interference	The government used the Natural Resources Ministry's environmental regulator to force private companies like LUKoil into sharing licenses and prevent aggressive bidding.
1.1.2.10 Third Order	Administrative Levers of the State	In the instance of LUKoil it was the Natural Resources Ministry's environmental regulator that blamed LUKoil for environmental

		violations and development delays.
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**17.2:** Elder, & Wall, (2006); Elder, (2006i) **2 articles**

Code	Theme	Notes
1.2 First Order	Diversion	Consolidation
1.2.2 Second Order	Diversion of Claims	Diversion of claims through questionable consolidation practise involving low valuation of target companies.
1.2.2.5 Third Order	Transactions with Self-Interest	LUKoil was seeking to consolidate its assets and employed aggressive valuation policies. Minority shareholders of targeted subsidiaries felt the valuation was inadequate.
1.2.2.3 Third Order	General Meeting	LUKoil being a large company with a significant clout was predicted by analysts as a potential winner in the conflict. However, a minority shareholder (Prosperity Capital Management) sought to boost its stake in the subsidiary to 25 percent in order to be in the position to block the merger at an upcoming general meeting.
1.2.2.7 Third Order	Self-Enforcement	LUKoil being a large company with a significant clout was predicted by analysts as a potential winner in the conflict. However, the minority shareholder (Prosperity Capital Management) sought to boost its stake in the subsidiary to 25 percent in order to be in the position to block the merger at the upcoming general meeting.

**18. Transneft:** Korchagina, (2006c); Levitov, (2006b) **2 articles**

Code	Theme	Notes
1.1 First Order	Management	Managing stakeholders, investigation into abuses by former managers.
1.1.2 Second Order	Ownership	Trading in preferred shares was cancelled because of an ongoing investigation into alleged abuses by former managers. The

		prosecutor general's office asked a number of brokerages to disclose the beneficiaries of Transneft.
1.1.2.1 Third Order	State Interference	The government, being a majority shareholder in Transneft, began an investigation into abuses of power by previous managers during privatisation of the company. The investigation might have stemmed from a conflict of a political nature. As part of the investigation, brokerages were asked to disclose information about the ultimate beneficiaries of the preferred shareholders.
1.1.2.2 Third Order	Inadequate Information	Detailed information about the owners of Transneft's preferred shares had to be disclosed because of an ongoing criminal investigation into abuses by former Transneft managers during the company's privatization. Deutsche UFG said that asking brokerages to disclose beneficiary owners of a company's shares "is an unprecedented case for the Russian stock market, which will likely further worsen sentiment surrounding Transneft shares.
1.1.2.12 Third Order	Litigation	The General Prosecutor's Office contacted the brokerages with a demand to disclose the identity of beneficiaries as a part of an ongoing criminal investigation. It is difficult to tell whether the investigation was a genuine effort to fight corrupt privatisation from years ago, or a way of punishing an influential

		investor who dared disagreeing with the state <sup>180</sup> .
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## 29. Novolipetsk (Parallel Coding) Humber, (2006j) 1 article

Code	Theme	Notes
1.2	Diversion	Management of subsidiaries.
1.1 First Order	Management	
1.2.2 1.1.2 Second Order	Diversion of Claims/ Ownership	The market forced Novolipetsk chairman to sell raw material suppliers to the parent group in order to avoid accusations of transfer pricing.
1.2.2.5 1.1.2.5 Third Order	Transactions with Self-Interest	The chairman of Novolipetsk sold raw materials suppliers that he owned to the group in order to address concerns of transfer pricing from the shareholders.

<sup>180</sup> The most interesting point however was the fact that disclosing who beneficiaries were, was predicted to would have worsened the sentiment on the stock market because of the constantly questioned legitimacy of privatisation.

1.2.2.7 1.1.2.7 Third Order	Self-Enforcement	The move to consolidate the raw materials suppliers was determined by the market pressures to increase transparency.
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### 30. Severstal (2 separate disputes)

#### 30.1: (Parallel Coding) Humber, (2006i); Humber, (2006j) 2 articles

Code	Theme	Notes
1.2 1.1 First Order	Diversion Management	Management of subsidiaries.
1.2.2 1.1.2 Second Order	Diversion of Claims Ownership	The market forced Severstal owner Mordoshov to sell raw material suppliers to the parent group in order to avoid accusations of transfer pricing.
1.2.2.5 1.1.2.5 Third Order	Transactions with Self-Interest	Mordoshov sold raw materials suppliers that he owned to the group in order to address concerns about the group's transparency. Previously, these types of assets were acquired by Kremlin insiders involving a series of transfer pricing schemes.
1.2.2.7 1.1.2.7 Third Order	Self-Enforcement	The move to consolidate the raw materials suppliers was determined by the market pressures to increase transparency as the company was preparing for either an acquisition or floatation.

**30.2:** Humber, (2006b); Humber, (2006g); Humber, (2006f); Humber, (2006e) **4**  
**articles**

<b>Code</b>	<b>Theme</b>	<b>Notes</b>
1.1 First Order	Management	Merger, management of stakeholders.
1.1.4 Second Order	Misimplementation	Severstal lost a bid to merge with Arcelor. Despite support from the board, Arcelor's shareholders turned down the offer.
1.1.4.2 Third Order	Inadequate Information	The European shareholders did not welcome Mordoshov's bid because they suspected foul play on the part of the unknown Russian businessman. Also, it was very easy for the competitors for Arcelor's assets (Mittal) to play the corruption card, i.e. a rich Russian who was not doing a great deal to introduce himself to shareholders, was a bit of a dark horse, and therefore was very likely to be/have been connected to the criminal world.
1.1.4.6 Third Order	Relationship-Based	Arcelor's shareholders voted down Mordoshov's offer despite recommendations from the board. Mordoshov may have had an informal agreement with the board of Arcelor promising their support in return for compensation. According to an official, Arcelor's board picked Mordashov over several other candidates, including rival Russian steel magnate Vladimir Lisin, due to "a record of close cooperation in several joint ventures and established trust. Mordashov's example could prove the key to long-expected consolidation in the Russian steel industry. "The sector is very closed right now" due to personal differences between leading steel companies' majority shareholders.
1.1.4.10 Third Order	Administrative Levers of the State	The government supported Mordoshov's bid for Arcelor. Mordoshov himself was very close to Kremlin and the president Putin. It could be assumed that the initial support of the Arcelor board was encouraged by the top Russian politicians even though Mordoshov himself denied that fact saying that

		Serverstal is a private entity.
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### 31. Evraz (2 separate disputes)

#### 31.1: Humber, (2006j) 1 article

Code	Theme	Notes
1.1 First Order	Management	Taxes
1.1.5 Second Order	Taxes	Evraz avoided taxes by using off shore traders to export domestic steel.
1.1.5.5 Third Order	Transactions with Self-Interest	Accusations of transfer pricing have dogged Russian metals producers as they seek to bring their business practices in line with Western standards. Last week, the Audit Chamber decided that the country's largest steelmaker, Evraz Group, used offshore traders to export domestic steel at below-market value, hence avoiding higher taxation.
1.1.5.12 Third Order	Litigation	Evraz avoided taxes by using off shore traders to export domestic steel. The Audit Chamber felt that Evraz was in the wrong and ruled against it.

#### 31.2: Smolchenko, (2006a) 1 article

Code	Theme	Notes
1.1 First Order	Management	Takeover.
1.1.2 Second Order	Ownership	The US authorities wished to scrutinize links between Abramovich and the Russian Government in relation to Evraz's bid for Oregon Steel.
1.1.2.1 Third Order	State Interference	Because the relationship between business and politics is so intertwined in Russia, the American authorities could use the investigation of that relationship as a tool to



		block the bid on political grounds. Equally so, the American authorities need to know what motivated the actions of the investor. It is suspected that Abramovich is linked to the Russian government, but the latter seeks to stop that news from spreading. If the national security is successfully passed, Evraz gets the green light for its \$2.3 billion purchase of Oregon Steel. The decision could be politically motivated and depends on the nature of the relationship between the businessman and the Kremlin.
1.1.2.2 Third Order	Inadequate Information	U.S. authorities were to examine Roman Abramovich's ties to the Kremlin before deciding whether to approve the sale of Oregon Steel to steelmaker Evraz Group, which the billionaire co-owns. The U.S. Treasury's Committee on Foreign Investment scrutinized Abramovich's ties to the Russian government as part of a national security review before clearing his \$2.3 billion bid for Oregon Steel. The report did not say when the review would take place. Abramovich, who also owns the Chelsea football club, is the governor of Chukotka. Governors are appointed by the Kremlin.

## 32. RusAl (4 separate disputes)

### 32.1: Mauldin, (2006a) 1 article

Code	Theme	Notes
1.2 First Order	Diversion	Consolidation, treatment of minority shareholders.
1.2.2 Second Order	Diversion of Claims	Allegations that RusAl and SUAL have bought out minority shareholders at below market prices.

1.2.2.5 Third Order	Transactions with Self-Interest	Valuation of minority stake is a central corporate governance issue. In this instance the companies have been accused of undervaluation despite their ambitions to go public on a foreign stock exchange. In protecting their interests, minority shareholders could play the IPO card which makes the management vulnerable to bad publicity.
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### 32.2: 'RusAI Named in \$2.8Bln Suit', (2006) **1 article**

Code	Theme	Notes
1.2 First Order	Diversion	Merger, bidding process.
1.2.2 Second Order	Diversion of Claims	RusAI allegedly conspired with the Nigerian president to tip the balance in favour of its less attractive bid for Alsccon in comparison with what BFI Group Devino was offering.
1.2.2.5 Third Order	Transactions with Self-Interest	RusAI allegedly conspired with the Nigerian president to tip the balance in favour of its less attractive bid for Alsccon in comparison with what BFI Group Devino was offering.
1.2.2.6 Third Order	Relationship-Based	The Russian company could conspire with the Nigerian president using Relationship-Based arrangements (probably non transparent) to secure support for its lower bid.
1.2.2.12 Third Order	Litigation	BFI Group Devino took the case to a US court as it apparently offered more for Alsccon. The Russian company argued that the US court lacked jurisdiction in this case.

### 32.3: 'RusAI Appoints 2 Outside Directors', (2006); Humber, (2006d); Humber, (2006a) **3 articles**

Code	Theme	Notes
1.1 First Order	Management	Financing.

1.1.2 Second Order	Ownership	RusAl disclosed its ultimate beneficiary because of a condition for a loan received from the EBRD and IFC. This in turn triggered a suit from a former business partner which had an impact on investor confidence.
1.1.2.2 Third Order	Inadequate Information	The EBRD and IFC used the loan as a means of pressurising the company to disclose its ownership structure. Also, possible foreign flotation and the issuance of the Eurobonds may have contributed to the decision. Additionally, the former business partner of Derepaska went for litigation to extract more money that he felt RusAl owed him. To address these concerns the company recruited two high profile non executive directors.
1.1.2.6 Third Order	Relationship-Based	Other former partners, brothers Simon and Peter Reuben, have settled claims against Derepaska out of court over the last year. This happened as Deripaska was seeking to improve corporate governance standards and transparency of RusAl and Basic Element.
1.1.2.8 Third Order	Third-Party Enforcement	The EBRD and IFC (the International Financial Corporation) used the \$150 million loan as a means to pressurise the company to disclose its ownership structure. Also, a possible foreign flotation and the issuance of the Eurobonds may have contributed to the decision to improve transparency of the company and its parent Basic Element. To address some of the corporate governance concerns the company recruited two high profile non executive directors.

1.1.2.12 Third Order	Litigation	The EBRD and IFC used the loan as a means of pressurising the company to disclose its ownership structure. It turned out that Derepaska was the sole shareholder of the group. This disclosure led to a former partner's legal complaint because he felt a debt to him had not been settled. He sued the company for \$3b in compensation.
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#### 32.4: Humber, (2006a) 1 article

Code	Theme	Notes
1.1 First Order	Management	Industry consolidation.
1.1.2 Second Order	Ownership	A possibility of a merger between two previously competing oligarchs.
1.1.2.6 Third Order	Relationship-Based	Derepaska and Vekselberg appeared to be burying the hatchet when they considered a possibility of a merger between their aluminium assets after years of bitter rivalry.
1.1.2.10 Third Order	Administrative Levers of the State	It has been suggested that the chances for a merger between Rusal and SUAL would be strengthened further should the new company allow the state to take a stake in the business. It was predicted that the Kremlin's support would bolster the merged company against possible legal claims.

#### 37. Eurocement: Humber, (2006c) 1 article

Code	Theme	Notes
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1.2 First Order	Diversion	Minority claims.
1.2.2 Second Order	Diversion of Claims	Allegedly, majority owners of Eurocement Group created the company with the aim of diverting profits away from the investment fund Russia Partners.
1.2.2.2 Third Order	Inadequate Information	The American registered fund upset the majority owners of the Eurocement group by blocking new share issue. The majority owners responded by refusal to send financial information to the fund. Subsequently, the majority set up the group and used internal pricing arrangements to divert the profits from the factories thus diverting profits away from the minority. The group was also under the investigation of the Federal Anti Monopoly Service for severe price hikes the previous year.
1.2.2.5 Third Order	Transactions with Self-Interest	The American registered fund upset the majority owners of the Eurocement group by blocking new share issue. The majority owners responded with a refusal to send financial information to the fund. Subsequently, the majority set up a group and used internal pricing arrangements to divert profits away from the factories and the minority. The group was also under the investigation of the Federal Anti Monopoly Service for severe price hikes the previous year.
1.2.2.8 Third Order	Third-Party Enforcement	The American fund recruited the services of A1 [a unit of Afla Group] to help it fight the case of expropriation on a particularly large scale in Russian courts namely the Moscow Arbitration Court.
1.2.2.12 Third Order	Litigation	The American fund recruited the services of A1 [a unit of Afla Group] to help it fight the case of expropriation on a particularly large scale in Russian courts namely the Moscow Arbitration Court.

**48. IKEA: (Parallel Coding)** Henry, (2006); 'Irregularities in the State of Regulations', (2006); Shuster, (2006); 'Mega Mall Tenants May Seek Damages', (2006) **4 articles**

Code	Theme	Notes
1.2 1.1 First Order	Diversion Management	Corporate raid.
1.2.2 1.1.4 Second Order	Diversion of Claims Misimplementation	It appears that the mall was closed by the local court for fire violations. The closure coincided with the busy Christmas period and may have been linked to an unidentified business group that allegedly benefited from the closure. If that was the case, this was a classic case of a corporate raid. Similarly, another IKEA mall was closed for safety concerns and reopened again after the company invested in local infrastructure.
1.2.2.4 1.1.4.4 Third Order	Unclear Rules	IKEA mall was closed for safety concerns and reopened again after the company invested in local infrastructure <sup>181</sup> . The regulations (in this case the fire code) are very vague and open to different interpretations. In other words if you are looking hard enough, you will find all sorts of violations - the very thing that makes corporate raids possible.
1.2.2.5 1.1.4.5 Third Order	Transactions with Self-Interest	It appears that the mall was closed by the local court for fire violations. The closure coincided with the busy Christmas period and may have been linked to an unidentified business group that allegedly benefited from the closure. If that is the case, this is a classic case of a corporate raid. Similarly, another IKEA mall was closed because of safety concerns and reopened again after

<sup>181</sup> The company invested in the local infrastructure, after which the governor intervened and ordered reopening.

		the company invested in local infrastructure.
1.2.2.8 1.1.4.8 Third Order	Third-Party Enforcement	It is very possible that a well connected local business group used the fire violation to put the competitor (IKEA) at a disadvantage. It is also very possible that the business group had more fundamental plans to do with the permanent closure of the mall. In these circumstances, based on the previous experience where the company invested in the infrastructure, IKEA had no choice but to negotiate a common solution with the stakeholders involved. The courts here were clearly used as an instrument at the disposal of the interested parties.
1.2.2.10 1.1.4.10 Third Order	Administrative Levers of the State	It is very possible that a well connected local business group used the fire violation to put the competitor (i.e. IKEA) at a disadvantage. The business group had more fundamental plans to do with the permanent closure of the mall. In these circumstances, based on the previous experience where the company was forced to invest in the local infrastructure, IKEA had no choice but to negotiate a common solution with the stakeholders involved. The courts were clearly used as an instrument at the disposal of the well connected interested parties.
1.2.2.12 1.1.4.12	Litigation	The fire inspection came up with 887 fire code violations further to an unrelated accident killing a 5 year old boy. Local

Third Order		politicians made populist claims promising to close the mall. The 30 day closure was ordered by the local court <sup>182</sup> .
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### Appendix 10: Major Russian Oligarchs

Name	Estimated wealth	Narrative
Roman Abramovich	\$28.7 billion	Abramovich made accumulated his wealth in the 1990s, when much of Russia's industry was purchased by government connected elite for a fraction of real value. The oligarch targeted major oil and aluminium assets. In 2005 he sold the Sibneft oil company to the Kremlin-controlled Gazprom for \$20.6 billion, allegedly, the biggest transaction in Russian corporate history.

<sup>182</sup> It is very possible that a well connected local business group used the fire violation to put the competitor (i.e. IKEA) at a disadvantage.



Name	Estimated wealth	Narrative
Vagit Alekperov	\$20 billion	Alekperov amassed his fortune by building up a huge stake in Russia's largest oil firm, LUKoil. The oligarch comes from oil-rich Azerbaijan, and towards the final days of the USSR was appointed First Deputy Minister of Fuel and Energy, a position he used to lobby for the merger of three major Russian oil producers. That firm became LUKoil and Alekperov assumed its presidency.
Vladimir Lisin	\$17.7 billion	Lisin sold a 7 per cent stake in his steel giant Novolipetsk to investors on the London Stock Exchange in 2005. The sale raised more than \$960 million and he still has an 83 per cent remaining. He has never meddled with politics and worked his way up from the shop floor. In 1993 he became involved with Novolipetsk.
Mikhail Fridman	\$16.5 billion	Fridmans' success is based on the banking-to-telecoms consortium Alfa Group, which he founded. He is one of the company's majority shareholders. Fridman has traditionally enjoyed good relations with the Kremlin but suffered a setback earlier this year when his country house was seized by the Government.
Viktor Vekselberg	\$16 billion	In 2004 Vekselberg spent an estimated \$148 million to acquire the second-largest collection of Russian Faberge Easter eggs in the world. His stated aim was to bring them back to the motherland so that ordinary Russians could admire their own cultural legacy. However, critics suggested that he might have been simply re-affirming his loyalty to the Kremlin. Vekselberg has a reputation for avoiding

Name	Estimated wealth	Narrative
		political debates. He began his business career in 1988 trading computers before going into business with a former classmate who had immigrated to the US. Oil is the main source of his wealth.
Oleg Deripaska	\$14 billion	Deripaska's competitors allege that he uses strong-arm tactics in hostile corporate takeovers. In 2001 he married Polina Yumasheva, former President Boris Yeltsin's granddaughter, and has long enjoyed close relations with Russia's political elite. He began his career in 1993 as a commodities trader.
Aleksei Mordashov	\$13.3 billion	Mordoshov owns a large stake in steel giant Severstal, which was privatised in 1993. He was finance director of the Cherepovets steel mill north of Moscow and in the 1990s was asked by the serving director to purchase the company's shares to prevent outsiders from buying into Severstal. Mordashov bought a large number of highly discounted shares for himself as well. He later turned Severstal into a powerful conglomerate, buying a car-maker, coal mines, railway companies and port facilities.
Vladimir Evtushenkov	\$12 billion	The source of Evtushenkov's wealth is the telecoms to real estate conglomerate that he controls called Sistema. In 1993 he helped set up the company which includes some of the most profitable assets that once belonged to the state in Moscow: the Russian capital's fixed-line telephone network, its principal mobile phone operator MTS (which is now Eastern Europe's biggest), the well known Children's World department store, and a large insurance company. Evtushenkov is widely regarded as one of the most erudite

Name	Estimated wealth	Narrative
		oligarchs, and has a doctorate in economics.
Vladimir Potanin	\$11.8 billion	Potanin won control of Norilsk Nickel in the 1990s from the mine's communist-era directors. In 1995 he helped devise a controversial loan-for-shares scheme whereby the Government sold off state enterprises at highly discounted prices in return for much needed bank loans. Potanin, a well established insider, benefited from the sales. In 1996 he became the country's first Deputy Prime Minister under Yeltsin, the highest office ever held by an oligarch.
German Khan	\$10.6 billion	Khan is regarded as one of the most reclusive, low-profile oligarchs. An allegedly close friend and business partner of fellow oligarchs Mikhail Fridman and Viktor Vekselberg, he owns a major stake in telecoms and banking consortium Alfa Group. Similarly to his associates and business partners Khan's speciality is oil. In the 1980s he met Fridman and several other future oligarchs while studying at Moscow's Institute of Steel and Alloys.
Viktor Rashnikov	\$8.5 billion	Rashnikov and a group of managers are believed to control 99 per cent of the shares in the iron and steel works in Magnitogorsk, Siberia, Russia's largest steel producer. Little is known about Rashnikov except that he was born and bred in Magnitogorsk and still lives there. It has been suggested that he worked his

Name	Estimated wealth	Narrative
		way up from the workshop floor to become the plant's general director in 1997.
Boris Ivanishvili	\$7.4 billion	Forbes' description of the secret of Ivanishvili's success could apply to many of other Russian oligarchs. In the 1990s "he bought firms for tens of millions of dollars and [later] sold them for billions of dollars." He has subsequently largely sold up and his money is primarily in investment funds.
Alisher Usmanov	\$5 billion	Usmanov, controls his corporate affairs through a holding company called Metalloinvest and has admitted to being totally enthusiastic about buying and selling shares.
Elena Baturina	\$3.8 billion	Baturina's wealth comes from a Moscow construction company called Inteko, which she owns. Her critics allege that she has been able to cash in on Moscow's construction boom because of the patronage of Yuri Luzhkov, the mayor of Moscow and her husband.
Rustam Tariko	\$2.9 billion	The source of Tariko's wealth is Russian Standard, a vodka-to-banking empire that has rapidly become one of Russia's most successful companies. Tariko appeared in the headlines when he was outed as the buyer of Pablo Picasso's Dora Maar with Cat. He paid more than \$150 million for the canvas. He was in London for the Russian Economic Forum in 2006, when he spoke on the theme of luxury as a Russian national idea.

Name	Estimated wealth	Narrative
Boris Berezovsky	\$1.6 billion	Berezovsky made his money in the 1990s by capitalising on his close contacts with then President Boris Yeltsin. His connections made possible for him acquire lucrative stakes in the Russian oil, car, airline and media industries, many of which he has since sold at substantial profit. Afraid of being jailed by the Kremlin, Berezovsky won political sanctuary in Britain where he now resides.
Igor Yakovlev	\$1.5 billion	Yakovlev, who appears to have built up a business rather than "inherited" it, is the owner of Russia's largest electronics retailer, Eldorado. Yakovlev built up his wealth by capitalising on Russians' growing demand for consumer durables. He founded the business with his brother Oleg in 1994 and has created an empire which has around 1000 stores in 600 Russian towns, as well as 85 stores in neighbouring Ukraine.
Shalva Chigirinsky	\$1.5 billion	Chigirinsky is one of Moscow's most successful property developers. He is also paying British architect Sir Norman Foster to design what will be Europe's tallest tower, to redevelop an entire island district in St Petersburg, and to create a huge entertainment complex in southern Moscow. Chigirinsky makes no secret of his dislike for Roman Abramovich, whom he accuses of having stolen half an oilfield. Abramovich denies the accusation.

Name	Estimated wealth	Narrative
Valery Oif	\$1.5 billion	There is very little information on Oif, apart from his age and marital status. This is surprising given that he is a senator representing a Siberian constituency in Russia's Federation Council. The source of his wealth is oil, and he was among those who established a company with Abramovich making plastic toys. He appears to have been one of his most important Abramovich's lieutenants ever since.
Mikhail Zingarevich	\$1 billion	Little is known about one of the directors of Russia's biggest forestry enterprise, the St. Petersburg-based Ilim Pulp. Zingarevich and his brother founded Ilim Pulp in 1992 with one other partner after working their way up through the hierarchy of various pulp mills. Today Ilim is one of the world's biggest timber firms, and the brothers comprise half of the company's board.
Boris Jordan and Stephen Jennings <sup>183</sup>	\$886 million and \$2.3 billion respectively	Jordan is an American investment banker of Russian origin while Jennings is a New Zealander. When the duo realised how cheaply Russia was going to sell off its major assets, Jordan and Jennings decided in favour of trying to benefit from the sales even though there were substantial risks attached. The two investors made a fortune.

<sup>183</sup> This is a rare case of foreign nationals fully exposing themselves to the risks and consequently large returns offered by opportunities of the early stage transition. For this reason the two investors are regarded as adopted Russian oligarchs even though they are nationals of other countries.

Name	Estimated wealth	Narrative
Nikolai Smolensky	\$148 million	Smolensky is the controversial young figure known as "baby oligarch". Aleksander Smolensky, his father, is an oligarch of 1990s who is no less controversial. The bank he once controlled, SBS-Agro, collapsed during Russia's financial crisis in 1998, leaving thousands of ordinary people without their life savings. While many Russian lives were ruined by the 1998 crash, Aleksander Smolensky somehow managed to prosper and created a new bank that his son briefly chaired before it was sold for \$325 million.
Mikhail Khodorkovsky	Dwindling	When Forbes published its first Russian rich list in 2004, Khodorkovsky headed it with an estimated \$23.6 billion. The original source of his wealth was oil, via the Yukos company that he built up during the 1990s. He is serving his eight-year sentence in a Siberian penal colony. His supporters contend that he was imprisoned because of his growing interest in politics, and his opposition to President Putin.
Vladimir Gusinsky	Dwindling	Gusinsky's case, similarly shows how dependent oligarchs are on the Kremlin's support. Gusinsky flourished under President Boris Yeltsin but subsequently his empire collapsed when president Vladimir Putin came to power. In the 1990s Gusinsky founded Media Most, a company that included the Segodnya newspaper, independent TV station NTV, and a banking and property empire. NTV became the Kremlin's target because of its highly critical coverage of the war in Chechnya. As a consequence, in 2000 Gusinsky was accused of embezzlement and money laundering and was forced into

Name	Estimated wealth	Narrative
		exile. He now lives in Israel.
Leonid Nevzlin	Dwindling	Nevzlin must be one of the few billionaires who is also wanted for murder. Like Khodorkovsky, he lost Kremlin's support but instead a prison now lives in Israel. He contends that the fraud and murder charges against him are completely fabricated for political reasons. He became a computer programmer working with Khodorkovsky in the late 1980s and remained the famous oligarch's right-hand man until 2001.
Paul Klebnikov	-	An American of Russian origin, Klebnikov was the editor of the Russian edition of Forbes, and it was he who in May 2004 published the country's first authoritative rich list. Less than two months after the list appeared in the public domain, Klebnikov was shot dead in a contract killing. His killers have never been found and some believe that he may have been killed because of his exposure of the famously secretive oligarchs.

Source: Edited from Osborn (2006).



