Introduction

Bruce Misamore was Chief Financial Officer and Deputy Chairman of Yukos, Russia’s largest oil company, from 2001 until 2005. While there, he introduced world-class standards in corporate governance, financial transparency and accounting. However, Misamore’s reforms were unwound when the company had its domestic assets seized by the Russian government after 2004 and Russia arrested its chief executive Mikhail Khodorkovsky. Misamore resigned in December 2005 and has since been instrumental in a global legal campaign to ensure that Yukos’s thousands of legitimate stakeholders receive compensation from the Russian government. Before joining Yukos, Misamore held senior-level finance roles with US oil companies PennzEnergy, Pennzoil Co and Marathon Oil. Misamore taught finance at Bowling Green State University in Ohio in the 1970s and says that the winters there are even colder than in Moscow.

Why did you choose to move to Russia and become Yukos’s CFO?

During my initial conversations with the CEO of Yukos, Mikhail Khodorkovsky, he made it clear that he wanted Yukos to become a transparent stakeholder-focused company. His aspiration was, in fact, to set the agenda for other Russian companies and oil companies globally, making Yukos a world leader for operational excellence, corporate governance, financial reporting, and investor relations. It seemed like a place where I would be able to make a major positive contribution, not just to the company itself, but also to the wider Russian economy.

What processes did you introduce to improve transparency and the quality of reporting and what did you find most questionable about Russian accounting practice?

Russian accounting had not really evolved since the Soviet era. It was primarily cash accounting, and they had no such thing as consolidation accounting. This meant that each individual legal entity was treated as a separate accounting entity and had to report to the government as such. This made it impossible to create a consolidated financial statement, which in turn caused a lack of sensible financial reporting and other practical problems. Michel Soublin, Yukos’ former CFO, and Khodorkovsky had already recognized that Russian accounting standards were inappropriate for a company like Yukos and had made a choice between International Financial Reporting Standards or US GAAP. Before I arrived, they had chosen the latter, in view of their plan to seek a listing for Yukos on a US stock exchange.

Were there any tensions between the use of US GAAP and statutory requirements Yukos had to also report using Russian accounting?

Yes. Despite the move to US GAAP, Yukos was still required to maintain Russian books for domestic tax and financial reporting purposes. As Russian accounts could not be consolidated, the eliminations you would normally make in consolidated statements needed to be tossed out the window, and accruals to reflect the true state of the business were non-existent. Because of the lack of inter-company eliminations, no reader of the Russian financials could have been properly informed of the true situation of the group as a whole.
What about the tensions over the reporting of oil and gas reserves? Does that remain a criminal offence in Russia?

In the Soviet Union the reporting of reserves was illegal, and technically that remains the case in Russia today. In the late 1990s and early 2000s, companies like Yukos, Lukoil, and TNK-BP elected to begin reporting in either International Financial Reporting Standards or US GAAP, which compelled them to report reserves. In the early Putin years, the government turned a blind eye to the existing Soviet-era law and didn’t bother to harass companies over this. The government seemed to recognize that, if Russian oil companies were going to raise capital in the international financial markets, they were going to have to comply with Western rules. However, after the Kremlin decided to renationalize a large portion of the country’s oil reserves, Yukos and other companies started to be harassed by the Ministry of Natural Resources over their reporting of reserves. While we certainly did not ignore these calls, we were committed to reporting our reserves, and did not believe that we would be subject to criminal sanctions.

Was Yukos one of the first Russian companies to adopt US GAAP?

Yes. We were the first Russian oil company to publish full US GAAP financial statements, including quarterly US GAAP financials. From 2002 onwards, there emerged a movement called “Yukos-ization,” in which other Russian companies sought to emulate what we had achieved in financial reporting and corporate governance. There were even seminars on it. The focus on transparent financial reporting and good corporate governance meant that Yukos had become recognized as a leader in financial reporting, corporate governance, and investor relations not just in Russia, but across the emerging markets. This was why I had gone to Russia—not only to improve Yukos but to drive forward standards across Russia’s industrial base.

However, when Yukos was attacked by the Russian government, most of the other companies backed off, especially on the corporate governance aspects. A key issue was over the identity of major shareholders. No other company in Russia had done that before we did. Companies that had been considering following us down that road scrapped their plans. Once the real Putin stepped forward, there was a significant regression in terms of corporate governance in Russia.

Why do you think the Russian government singled out Yukos?

There were several factors. In April 2003, we announced a merger with Sibneft, another leading Russian oil company, with Yukos as the dominant partner. That would have created by far the dominant Russian oil company and one of the biggest oil companies in the world. While Mr Putin originally supported the deal, he may later have seen this as a threat.

He also had a growing, though not at that stage explicit, desire to renationalize the commanding heights of the Russian economy—and particularly to exert more control over the country’s resources. He also may have resented the fact that Yukos had a number of Americans in senior roles and that its principal shareholder group was having talks with major Western oil companies about possible share interests and cross-shareholdings.

Another factor was that Mr Khodorkovsky was supporting reform candidates in the 2003 Duma elections. Mikhail was doing that, among other things, out of concern that Mr Putin was poised to reverse many of the reforms put in place by Boris Yeltsin during the 1990s.

Did relations between Yukos and the Russian government deteriorate thenceforth?

In December 2003, the Russian government singled out Yukos for retroactive reinterpretation of Russian tax law, and the group started to be hit with massive tax bills. Initially, there was a bill of over US$3bn, but ultimately this rose to over US$30bn. The Kremlin got court judgments against us, freezing all assets, which made it impossible for us to pay the taxes by selling assets, and started removing all cash from the company.
We continued the legal battle with the government, but by late 2004 it had become clear that they would prevail, at least with respect to Yukos’ Russian assets. The most significant blow came when the Russian government auctioned off Yukos’s biggest subsidiary, Yuganskneftegaz, to pay some off the alleged back taxes. The Russian government ultimately expropriated all of Yukos’s Russian assets through a legally questionable bankruptcy process, and the assets ended up with the state-owned companies Rosneft and Gazprom.

Were you able to do anything about this?

In early December 2004, we appointed the Houston-based law firm Fulbright & Jaworski, who represented us in the US Federal bankruptcy court. The court issued an injunction against the Yuganskneftegaz auction. However, the Russian government totally ignored this injunction. We had intended to use the US bankruptcy as a means of protecting the assets of the entire company for the sake of its stakeholders—including employees, legitimate creditors, and the 50,000 plus shareholders who have to date received zero compensation from the Russian government.

But in March 2005 the US Bankruptcy Court determined that, since the Russian government was the largest creditor and the Russian government was not co-operating in the bankruptcy process, it would be impossible for the bankruptcy to conclude successfully. This meant the case was discontinued and we lost the protection of the US bankruptcy courts. We then started looking around for alternative ways of protecting the remaining assets, believing that while Yukos’s international assets could probably be protected, its Russian domestic assets probably could not.

When and why did you leave Russia?

In late November 2004 I was at a meeting in London and received a phone call telling me that I should not go back to Russia because I risked being arrested upon my return. I never went back and, indeed, around that time virtually every member of the management committee of Yukos had left Russia never to go back. I arrived in Houston December 4 and we began the bankruptcy process in the United States.

Under the circumstances, was it hard to focus on your original mission of improving standards of corporate governance etc at Yukos?

The focus had to change. We had a major battle on our hands trying to save the company and to convince the Russian government that we were good corporate citizens. We tried all kinds of tax settlement negotiations throughout 2004, including bringing in some very high profile international political figures. These included the former prime minister of Canada, Jean Chrétien, who employed the assistance of some other prominent world leaders to try to reach a settlement. They all had conversations with Mr Putin, who made promises, which he failed to deliver.

What happened to Mr Mikhail Khodorkovsky?

In October 2003 Mikhail was arrested and charged on a personal basis for alleged crimes, primarily related to a fertilizer company that his group had acquired in the mid-1990s. Since his arrest, Mikhail has not been out of jail for a single minute. He was, of course, found guilty of all charges and was sentenced to prison in Eastern Siberia. He is now on trial again in Moscow on phony charges, primarily limited to stealing all of Yuko’s oil production from 1998–2003. That trial is a political show trial and will take several months.

What are your chances of securing compensation for Yukos shareholders from the Russian government?

During 2004 and 2005 we scoured the world during for legal structures to protect Yukos’s international assets and we found a structure in the Netherlands called a Stichting, a Dutch “foundation” structure. We
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now have formed two stichtings in which we have put all of Yukos’s international assets. The Stichtings have served us extremely well.

We are still battling off attacks from Rosneft and other entities and fronts of the Russian government, which keep trying to seize those assets.

However, we have won virtually every meaningful court case outside Russia, including a key victory in October 2007, which said that the Russian bankruptcy would not be recognized in the Netherlands. There is a strong chance that sizeable verdicts will be levied against the Russian government. In January 2009, the main Yuko case was admitted to the European Court of Human Rights.

However, it is going to be years before any money is collected for the parties that have been harmed. If the cases that are currently being heard under the European Energy Charter Treaty and in the European Court of Human Rights were to rule against Russia, it would hopefully serve as a wake up call for the country.

This is the main reason I continue to be involved. The Russian public and political community need to understand that expropriation is not the way to improve the economy.

What is the outlook for the transparency of financial reporting in Russia?

Through its intimidation campaign, the Russian government has compromised the move to more transparency in Russian entities, including the disclosure of major shareholders. This has led to questionable disclosure by a lot of Russian companies. However, whenever Russian companies are seeking to raise money in international capital markets, they will have to provide reasonable financial statements. I think that even Mr Putin understands that.

What is the outlook for the Russian economy?

Russia has become an autocracy and this is bad news for the economy. It means that Russian companies will never get a consistently strong inflow of Western capital. This is very different from other economies in Eastern Europe. Few other former Soviet or Warsaw Pact republics, other than Belarus, have regressed as far as Russia has. As a result, the Western banking crisis has had a far bigger impact on Russia. There’s been a massive flight of capital out of Russia and a more pronounced stock market crash there, a crash in the rouble and a significant decrease in purchasing power.

What is your advice to someone from a developed country who is considering taking on a CFO role in a Russian company right now?

I would not want to share my talents with Russia today because the situation there is far, far different from what it was like when I went there in 2001. Until the Russian government explicitly supports transparency in its businesses and gets a handle on government corruption, I don’t think anyone should waste their time in Russia. There’s currently no sign of that happening.

Are there lessons for transparency in other emerging markets?

The only way for emerging market companies to achieve the kind of results they want is through financial transparency and good corporate governance. This also needs to be understood by the politicians and others within those countries. In India, because of its British background, there is more transparency. However, I believe that China will achieve less economically in comparison with what it could otherwise achieve because of the country’s apparent failure to encourage transparency.
More Info

Books:


See Also

Best Practice

- Political Risk: Countering the Impact on Your Business

Checklists

- Defining Corporate Governance: Its Aims, Goals, and Responsibilities
- International Financial Reporting Standards (IFRS): The Basics
- Key Accounting Standards and Organizations
- The Ten Accounting Principles
- Understanding the Key Components of GAAP: The Continuing Concern Concept

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