

• Author: [Maximilian Hess](#)

[How Transneft lost its legal battle against Sberbank](#)



Russian state energy companies, particularly the big three of Rosneft, Gazprom and Transneft, play an outsized role in Russia's economic and political life. The three are controlled by longstanding allies of President Vladimir Putin: Gazprom by Alexei Miller, Putin's [former subordinate](#) at St. Petersburg's External Relations department; Rosneft by Igor Sechin, Putin's [chief-of-staff](#) during his time in St. Petersburg; and Transneft by Nikolai Tokarev, Putin's former KGB [colleague](#) in East Germany. Their influence is so strong that the courts regularly bend to their will. However, a [ruling](#) on August 23rd by Moscow's Ninth Arbitration Court showed that limits on their power do indeed exist, if only informally.

The arbitration court was hearing an appeal brought by Sberbank, majority-owned by the Russian state, against state-owned pipeline monopoly Transneft. This was a follow-up from a previous [June ruling](#) in Transneft's favour by the Moscow Arbitration Court. The June ruling was part of a well established trend in Russia's legal system: one of the Big Three - Rosneft/Gazprom/Transneft - launches legal proceedings against a political or economic opponent, and the court issues a judgement neatly in line with the complaint.

This formula, it is worth noting, is not limited to the Big Three. Other high-profile trials not involving the three firms in recent years have also involved disconcerting courthouse power plays, most prominently [those](#) used to bar opposition figure Alexei Navalny from participating in the presidential elections. Another example was [the frankly absurd acceptance of legal claims](#) used to extract tax rebates from Bill Browder's Hermitage Capital and the [posthumous conviction](#) of Browder's lawyer, Sergei Magnitsky.

The Transneft and Sberbank dispute in question emerged from a [currency hedging agreement](#) Transneft entered into in 2013 "with the aim of reducing corporate bond servicing costs". The deal was extremely straightforward, at least in relation to the often complex world of derivative markets. In essence, Transneft bought the right to sell US\$2bln to Sberbank up until September 2015 in exchange for 65bln rubles, essentially locking in an exchange rate of 32.5 rubles to the dollar. To cover its risk, Sberbank also purchased the right to buy US\$2bln from Transneft for 65bln rubles over the same time period.

By the time the options expired, the ruble had weakened substantially. The [exchange rate](#) was roughly 66 rubles to the dollar. As a result, Sberbank exercised the option, buying US\$2bln from Transneft for 65bln rubles, leaving Transneft nearly 67bln rubles (US\$1.13bln) down given that US\$2bln cost 132bln rubles on the open market at the time.

Transneft was not pleased that its hedging strategy, aimed at protecting against a rise in the ruble's value, had backfired. Only in January 2017 did it launch the lawsuit against Sberbank, demanding the options be rendered invalid. Transneft argued that Sberbank did not broker their derivatives transaction fairly as Transneft argued it did not have sufficient expertise to evaluate the deal. Transneft Vice President furthermore [claimed](#) that the deal was not sold as a currency hedge but as a way to reduce the cost of debt servicing.

While Transneft did initially receive a net premium for the derivatives transaction, any first-year finance student would know such transactions are not a standard tool for reducing debt servicing costs: They are arguably among the most common and straightforward way for companies to hedge currency risks. Underlining the absurdity of Transneft's sudden claim that it did not understand the deal was that Transneft and

Sberbank had entered into [31 such agreements](#) previously.

The 16-month delay between Transneft's suit and its losses on the option has not been explained, either. The viability of Transneft's suit relied on the arbitration court's [application of a three-year statute of limitations](#), rather than the standard one-years statute in such cases. Furthermore, the June ruling released Transneft from responsibility for its own actions. In other words, the court accepted Transneft's specious legal arguments in full, [reportedly](#) due to Tokarev's influence.

However, the June ruling had implications far beyond the 67bln rubles Sberbank was ordered to pay back to Transneft. It demonstrated that the Big Three energy companies could even take on key state financial institutions and bend the judiciary in their favour to do so. The Central Bank, [arguably](#) the best run government institution in Russia, also reacted negatively, [concerned](#) the ruling would set a legal precedent undermining other derivatives contracts.

Perhaps due to these concerns, it appears the Kremlin intervened, with RBC [reporting](#) that Deputy Prime Minister Arkady Dvorkovich lobbied Tokarev to reach a settlement agreement with Sberbank, which may have sent the message to the appellate court to rule in Sberbank's favour. Additionally, Sberbank [reported it never set aside reserves](#) following the June ruling, likely an indication it received assurances it would ultimately not have to pay.

Unfortunately, another court ruling, also on 23 August, demonstrated how much the courts continue to bend to the will of Rosneft, Transneft and Gazprom. This was when the Bashkortostan Arbitration court [ruled in Rosneft's favour](#) in relation to its [latest preposterous lawsuit](#) against Sistema. In effect, the ruling [holds that](#) Sistema must pay Rosneft 136bln rubles (US\$2.3bln) for its management of Bashneft, expropriated from it three years prior [at Rosneft's insistence](#).

Sistema now risks losing control of its most valuable remaining asset, the mobile service provider MTS. Although Putin subsequently [called for](#) an 'amicable agreement' between the two companies, the fact that Rosneft is even pursuing Sistema again three years after the expropriation, even [setting up the arrest](#) of former economy minister Alexei Ulyukayev to do so, demonstrates the lack of accountability for its actions.

August 23 appears to have sent a clear message. Large state energy businesses have the right to take spurious legal actions to boost their balance sheets at the expense of private firms - but not at the expense of other key state enterprises.

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