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SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: **BARBARA R. KAPNICK**

PART 39

Index Number : 106539/2001

GUS CONSULTING GMBH

VS.

CHADBOURNE & PARKE LLP.

SEQUENCE NUMBER : 022

SUMMARY JUDGMENT

INDEX NO. 106539/01

MOTION DATE _____

MOTION SEQ. NO. 022

MOTION CAL. NO. _____

its motion to/for _____

PAPERS NUMBERED _____

Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...

Answering Affidavits — Exhibits _____

Replying Affidavits _____

Cross-Motion: Yes No

Upon the foregoing papers, it is ordered that this motion

FILED

JAN 14 2010

NEW YORK
COUNTY CLERK'S OFFICE

**MOTION IS DECIDED IN ACCORDANCE WITH
ACCOMPANYING MEMORANDUM DECISION**

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
FOR THE FOLLOWING REASON(S):

Dated: 1/8/10


BARBARA R. KAPNICK J.S.C.
 J.S.C.

Check one: FINAL DISPOSITION NON-FINAL DISPOSITION

Check if appropriate: DO NOT POST REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 39

-----X
GUS CONSULTING GmbH, f/k/a "CREDITANSTALT
INVESTMENT BANK, AG", CIS EMERGING FUND
LIMITED, ZAO FINANCIAL PARTNERS, AND
ZAO CREDITANSTALT-GRANT,

Plaintiffs,

-against-

CHADBOURNE & PARKE LLP,

Defendant.

-----X
BARBARA R. KAPNICK, J.:

DECISION/ORDER
Index No. 106539/01
Motions Seq. Nos. 022,
023 and 024

FILED
JAN 14 2010
NEW YORK
COUNTY CLERK'S OFFICE

Motions sequence numbers 022, 023 and 024 are consolidated for disposition.

In this action, plaintiffs GUS Consulting GmbH f/k/a Creditanstalt Investment Bank AG ("CAIB"), an Austrian investment bank, and its affiliates, CIS Emerging Fund Limited ("CISEF"), ZAO Financial Partners ("FP"), and ZAO Creditanstalt-Grant ("CA-Grant")¹ seek to recover compensatory and punitive damages, together with interest, costs and attorneys' fees, against defendant Chadbourne & Parke LLP ("Chadbourne") for alleged legal malpractice.

¹ CISEF, FP, and CA-Grant shall collectively be referred herein as the "CAIB Affiliates".

The three CAIB Affiliates were established by or on behalf of CAIB to facilitate CAIB's investment activities within the Russian Federation. The Second Amended Complaint alleges, *inter alia*, that Chadbourne provided negligent and erroneous advice on the structure of an investment vehicle. The structure was used by the CAIB Affiliates to enable clients of CAIB to invest in certain restricted securities traded on Russian exchanges, including shares of a large Russian natural gas concern called RAO Gazprom ("Gazprom").

The Second Amended Complaint also alleges that Chadbourne "failed to advise CAIB adequately about the consequences, should the SP Structure be deemed illegal."

Defendant now moves, under motion sequence number 022, pursuant to CPLR § 3212 for an order granting summary judgment dismissing the Second Amended Complaint in its entirety, on the ground that plaintiffs cannot establish the elements required to recover for professional malpractice, or, in the alternative, dismissing plaintiffs' claim for punitive damages on the ground that the facts relied upon by plaintiffs do not demonstrate the required degree of culpable conduct.

After oral argument on defendant's motion for summary judgment was held, plaintiffs moved, under motion sequence number 023, to supplement the record in this matter to include the Affidavit of Helmut Horvath, a member of the management board of CAIB, in order to address certain issues which plaintiffs claim were raised for the first time after their opposing papers were submitted.

Plaintiffs subsequently moved in October of 2009, under motion sequence number 024, to supplement the record a second time in order to include a certified copy of a resolution by Investigator Dubov of the Russian Tax Police.

A non-certified copy of the document produced by plaintiffs was submitted as an exhibit to defendant's initial motion. Defendant correctly argued at the time that the document was inadmissible and should not be considered by the Court. Plaintiffs now seek to correct that evidentiary defect.

The motion to supplement the record to include the Horvath Affidavit is granted, in the discretion of the Court, in the interests of deciding the matter on the merits based on a full record.

However, the second motion to supplement the record to include a certified copy of the resolution is denied, since the motion was made over ten months after oral argument was held on motion sequence number 022, and plaintiffs have not presented a sufficient excuse why a certified copy was not included in the initial record.

Background

The Second Amended Complaint alleges that in April 1996, CAIB acquired the assets of a Russian joint stock company of the closed type which was engaged in securities brokerage activities. CAIB established CA-Grant in connection with that acquisition.

Attorneys associated with a Denver, Colorado law firm, Holme Roberts & Owen LLP ("Holme Roberts"), worked on the acquisition and undertook to represent CAIB and CA-Grant in various matters related to their Russian activities. In 1996, CAIB allegedly asked Holme Roberts to suggest a legal structure that would allow CAIB's clients to invest in certain Russian securities, including Gazprom, and to minimize the Russian tax consequences for such investments.

Plaintiffs claim that Holme Roberts, through Margaret B. McLean, Esq. and other attorneys at that firm, ultimately advised them to invest their clients' money in Gazprom and other Russian

securities utilizing a derivative investment product or vehicle called a "Simple Partnership Structure" (the "SP Structure"). CAIB purportedly relied on that advice in setting up the SP Structure in 1997 and in offering the investment opportunity to its clients. CAIB clients thereafter invested funds through the SP Structure.²

Holme Roberts' "Moscow team" allegedly joined Chadbourne in 1998 at or about the time Holme Roberts closed its Moscow office. Plaintiffs allege that during and after the transition of attorneys and clients from Holme Roberts to Chadbourne, Chadbourne undertook to provide CAIB with a legal opinion addressing the SP Structure's legality under Russian law, and specifically Decree No. 529, which was issued by President Boris Yeltsin in May of 1997 shortly after CAIB implemented the SP Structure. Decree No. 529 limited the extent to which foreign entities could own Gazprom shares.

Chadbourne issued a Risk Assessment Letter dated February 13, 1998, which plaintiffs claim adopted Holme Roberts' prior work and advised CAIB that the SP Structure did not violate Russian law and should continue as CAIB's investment vehicle for restricted Russian securities.

² A separate action brought by plaintiffs against Holme Roberts is pending in Colorado.

CAIB claims to have relied on this advice in subsequently investing large sums of CAIB's money, as well as its clients' money, in Russian securities through the SP Structure.

There is no dispute that Chadbourne periodically responded to plaintiffs' further inquiries about the SP Structure in 1998 and 1999. Defendant contends that plaintiffs also received extensive and ongoing advice about problems with the SP Structure, including the potential risks of using the SP Structure, from three of the world's largest accounting firms.

Plaintiffs contend that Chadbourne's advice was both wrong and negligent because the SP Structure ran afoul of Decree No. 529 and other Russian laws, including Russian tax laws.

Plaintiffs further claim that Chadbourne later realized that its advice was erroneous, but still failed to notify CAIB or the CAIB Affiliates. Moreover, plaintiffs claim that defendant failed to adequately warn CAIB about the potentially adverse consequences in the event that the SP Structure was deemed illegal. See, *National Enterprises Corp. v Dechert Price & Rhoads*, 246 AD2d 481 (1st Dep't 1998); *Campbell v Rogers & Wells*, 218 AD2d 576 (1st Dep't 1995).

Defendant disputes plaintiffs' claim that its legal advice was erroneous, and contends that it warned plaintiffs of the risks associated with the SP Structure. Specifically, in a letter dated February 13, 1998 to Kyle Shostak, General Counsel of CA-Grant, Rashid Sharipov, an attorney in Chadbourne's Moscow office, wrote, in relevant part, as follows:

The SP Structure has been developed to comply with existing Russian legislation to the maximum extent possible. It has, however, several drawbacks and some unresolved concerns, as identified below, that could be considered when making the final investment decision with respect to the structure.

1. The SP Structure is aggressive because it is not based on a generally accepted concept of a Russian legal entity. The pass-through nature of the structure, popular in the West for tax structuring purposes, may not be well received by Russian tax authorities. Because of the abuses of the joint activity structures during the early days of privatization voucher actions, the structure may be viewed by tax authorities with suspicion as a tax avoidance device. For the SP Structure to benefit from the passthrough characteristics, the partners must follow precisely the extensive accounting regulations on bookkeeping, reporting and compliance for the Simple Partnership.

2. Because the volume of the investment funds in the SP Structure may be very large, the SP Structure may raise questions with regulators and tax authorities alike. Given the magnitude of the operation and given that CAG is regulated by the Federal Securities Commission certain risks exist that investment in the SP Structure may be subject to greater regulatory scrutiny. Suffice it to say, given the capital infusion volumes anticipated and made to date, it may be difficult for CAG and the SP Structure to keep a low profile.

3. The SP Structure is based on the premise that the partners would contribute the capital to the SP and that capital would be used for investment in the Restricted Shares. To return the principal and gain, CISEF from time to time would request the redemption of a part of

its interest in the SP Structure. Such redemption is permissible under Russian law. Yet, frequent and large movements of money in and out of the SP Structure may raise questions and would make the SP Structure more noticeable. To the extent possible, it would be advisable to manage the cash flow in and out of the SP Structure.

4. While we believe that the SP Structure is not inconsistent with the provisions of Decree #529 on the trading of Gazprom Shares for the reasons stated in section II above, it appears that the real intent of Decree #529 was to limit the ability of foreign investors to purchase Gazprom Shares at domestic prices that are currently significantly lower than international prices.

... It is likely that the government in its attempt to curtail foreign access to the Restricted Securities market will enact additional regulations which could render the SP Structure inoperative.

Plaintiffs concede, as the documentary evidence demonstrates, that Chadbourne informed CAIB that certain civil tax or political consequences might arise from the SP Structure, but plaintiffs now contend that Chadbourne never specifically and/or fully advised them as to the possible criminal consequences.³ Plaintiffs also argue that in the deposition testimony of Mikhail Rosenberg, a

³ In affirming a prior determination of this Court, the Appellate Division, First Department held that "[d]efendant sufficiently demonstrated that the advice it gave in the course of its allegedly negligent representation was framed, in this malpractice action, as the sole cause of plaintiffs' injury in Russia." *Creditanstalt Inv. Bank AG v. Chadbourne & Parke LLP*, 39 AD3d 201 (2007). However, that decision related to the First Amended Complaint, and did not address the ultimate merits of the case. Plaintiffs subsequently filed their Second Amended Complaint to include, *inter alia*, their claim that defendant failed to warn plaintiffs of the possible criminal consequences.

senior partner at Chadbourne & Parke in Moscow, he "rattled off" all sorts of criminal consequence that, if contained in the advice given by Chadbourne at the time, would have caused plaintiffs to shut down the SP Structure. Plaintiffs further claim that had Mr. Rosenberg properly supervised the junior associates at Chadbourne who, unbeknownst to plaintiffs, were the ones giving them this crucial legal advice at the time, they would have shut down the SP Structure.

In 1999 and 2000, Russian authorities commenced a criminal investigation against the management of CAIB and the CAIB Affiliates, arrested the CAIB Affiliates' securities, and seized bank accounts, including accounts holding millions of Gazprom shares. The authorities also seized the CAIB Affiliates' corporate seals, effectively terminating their ability to conduct business in Russia on CAIB's behalf. CAIB was thus ultimately forced to shut down all of its businesses and operations in Russia.

Plaintiffs allege that had Chadbourne properly advised CAIB about the SP Structure's illegality under Russian Law, and in particular - Decree No. 529 and the Russian tax laws, and the risks of employing and continuing to employ such a structure, CAIB would have taken all steps necessary to achieve compliance with Russian

law and to eliminate the risk of being forced to close its Russian operations.⁴

Defendant, however, contends that the evidence demonstrates that the raid by the Tax Police was not the result of the use of the SP Structure, but rather the culmination of a series of events involving one of plaintiffs' employees, Dmitri Arkhipov, whose employment was scheduled to be terminated on May 31, 1999.⁵ Arkhipov allegedly stole 108 million of the 190 million Gazprom shares held by plaintiffs for their customers in the SP Structure during a seven-week period in April and May 1999. Defendant contends that plaintiffs' own auditors later determined that plaintiffs' inadequate business controls had enabled Arkhipov to commit these thefts without being detected.

⁴ Mr. Horvath claims that

[in] 1998, CAIB was prepared to change or terminate the SP Structure if we regarded the attendant risks as too great. Indeed, that was the very purpose of my requesting that a comprehensive risk assessment be undertaken. Accordingly, if Chadbourne had advised CAIB that continued use of the SP Structure would expose CAIB to a risk of criminal consequences, including Russian Tax Police investigations that would expose individual employees to criminal prosecutions, CAIB would have made certain that use of the SP Structure ceased immediately.

⁵ Mr. Arkhipov's position was eliminated as a result of staff reductions necessitated by the banking crisis in Russia which began in August 1998.

According to defendant, a security video camera recorded a meeting between Arkhipov and an officer of the Tax Police which was held in plaintiffs' offices the weekend before Arkhipov's employment was to be terminated. The raid of plaintiffs' offices took place on June 1, 1999, immediately following Arkhipov's last day of employment, and again in October 1999.⁶

Defendant contends that Arkhipov, who allegedly accompanied the Tax Police on June 1, 1999, corruptly enlisted the Tax Police to conduct the raid in order to deter discovery of his thefts.

Although plaintiffs allege that the Tax Police initiated the criminal investigation into plaintiffs' investment activities in Russia and seized the remaining Gazprom shares held by plaintiffs in February 2000, there is no dispute that the Russian authorities never formally brought any criminal proceedings against plaintiffs or their employees in connection with the SP Structure. Thus, the Tax Police never made any formal determination that the SP

⁶ It was during the second raid that most of the contents of the office, including the business seals, were seized.

Structure was, in fact, illegal.⁷ The seized Gazprom shares were ultimately released.

Discussion

Defendant moves for summary judgment dismissing the Second Amended Complaint in its entirety, on the grounds, *inter alia*, that plaintiffs cannot demonstrate that Chadbourne's advice caused plaintiffs' alleged injuries.⁸

It is well settled that

[r]ecovery for professional malpractice against an attorney requires proof of three elements: "(1) the negligence of the attorney; (2) that the negligence was the proximate cause of the loss sustained; and (3) proof of actual damages" (citation omitted). It requires the plaintiff to establish that counsel "failed to exercise the ordinary reasonable skill and knowledge commonly possessed by a member of the legal profession" and that "'but for' the attorney's negligence" the plaintiff would

⁷ There is no dispute that the applicable Statute of Limitations for bringing charges in connection with the SP Structure ran in 2006 and would now bar a prosecution against plaintiffs or their former employees in connection with the SP Structure.

⁸ In addition, defendant argues that plaintiffs cannot establish any damages relating to the destruction of their business, as opposed to professional fees paid, because plaintiffs have not disclosed any evidence nor provided any expert disclosure as to the value of the business and the destruction of their property when the initial raid occurred. Rather, plaintiffs' Expert Disclosure reveals that plaintiffs intend to rely on the testimony of an accountant/appraiser, Thomas Blake, who will testify as to the hypothetical current value of their business.

have prevailed in the matter or would have avoided damages (citations omitted).

Ulico Casualty Co. v Wilson, Elser, Moskowitz, Edelman & Dicker, 56 AD3d 1, 10 (1st Dep't 2008). See also, *McCoy v Feinman*, 99 NY2d 295 (2002).

"To succeed on a motion for summary judgment dismissing a cause of action alleging legal malpractice, the attorney must establish, through the submission of evidentiary proof in admissible form, that the plaintiff is unable to prove at least one of the essential elements of the cause of action (citations omitted)." *Fireman's Fund Ins. Co. v Farrell*, 57 AD3d 721, 722 (2nd Dep't 2008).

Defendant argues that plaintiffs cannot meet their burden in this case of showing that 'but for' any act or omission by Chadbourne plaintiffs would not have sustained their alleged damages, because any injury to plaintiffs was caused by the actions of plaintiffs' own employee (i.e., Arkhipov), by the illegal actions of Russian government officials, and/or by illegal conduct on the part of plaintiffs.

Defendant further argues that plaintiffs are collaterally estopped from re-litigating issues they had a full and fair

opportunity to litigate and that were necessarily decided after a ten-day hearing before an Arbitrator, [the "Dart Arbitration"] In the Matter of LCIA Arbitration No. 2371, held in the London Court of International Arbitration in or about February 2007.⁹ Defendant claims that the sole Arbitrator, Simon Crookenden QC, determined, *inter alia*, that: (i) the SP Structure did not violate Russian law; (ii) the Tax Police raid was caused by Arkhipov to cover up his theft of the 108 million Gazprom shares; and (iii) plaintiffs' own negligence caused or otherwise permitted the theft to occur.

Plaintiffs dispute that the issues decided by the Arbitrator regarding the legality of the SP Structure are the same as the issues presented here, and argue that there is, therefore, no basis for collateral estoppel to be applied. *See, Braunstein v Braunstein*, 114 AD2d 46 (2nd Dep't 1985); *lv. to app disms'd* 68 NY2d 453 (1986). Plaintiffs claim that the Arbitrator was called upon to address the legality and enforceability under Decree No. 529 of only two specific contract provisions.¹⁰

⁹ The binding arbitration was commenced by DCL-KF Corporation ("DCL") which is a vehicle for investments of the Dart Group of companies, including Dart Container, who were investors in plaintiffs. DCL sought to recover shares (or the value of the shares) which were stolen by Arkhipov, claiming that plaintiffs were responsible for the safekeeping of the shares. DCL also sought to recover dividends that had not been accounted for on other shares held on the Dart Group of Companies' behalf.

¹⁰ Plaintiffs contend that the Arbitrator did not address what they contend are the 'key' issues raised in their Second Amended Complaint; i.e., whether or not Chadbourne attorneys negligently failed to warn plaintiffs of the possible criminal

The Arbitrator ultimately found that CISEF was in breach of the Russian Equities Investment Agreement ("REIA") by "failing to exercise due care to maintain the registration of the Gazprom shares held in the SP Structure for DCL and to safeguard DCL's funds and investments," and "in distributing the shares and funds held in the SP Structure otherwise that [sic] in accordance with the pro-rata entitlements of investors and in failing to wind down and distribute to DCL its share of such shares and funds."

However, the Arbitrator also found that

[t]he SP Agreement in so far as it provides for the profits or the proceeds of sale of the Gazprom shares to be credited mainly to CISEF is not in breach of Decree 529 which is concerned with the acquisition of title rather than any entitlement to the income from or the proceeds of sale of shares ... I am not satisfied, therefore, that the SP Structure ... was illegal in accordance with Russian law.

Thus, the Arbitrator did, in fact, make a specific finding as to the legality of the SP Structure.¹¹

and dire consequences for their Russian business if Russian authorities took action against plaintiffs because of their use of the SP Structure; and whether or not Chadbourne was negligent in their supervision of the associates who advised plaintiffs.

¹¹ Defendant argues that plaintiffs were well aware of the potential collateral estoppel effect of the Arbitrator's decision, as the Arbitrator himself noted as follows:

I was informed that proceedings in other jurisdictions are continuing or contemplated including the claim by CAIB against Chadbourne & Parke referred to above. In these circumstances, the Respondents submitted that it

Plaintiffs, however, argue that even if they are estopped from claiming herein that the SP Structure was illegal and that the raid by the Tax Police, which plaintiffs concede was a relatively routine occurrence in Russia at the time, was caused by Chadbourne's erroneous advice, plaintiffs can still demonstrate that "but for" Chadbourne's negligence they would not have sustained the damages claimed herein.¹²

Specifically, plaintiffs contend that the raid (no matter what precipitated it) segued into a prolonged Tax Police investigation and threatened criminal prosecution of senior CAIB executives, as a result of questions relating to the SP Structure.

Plaintiffs further contend that they would not have relied on that investment vehicle had Chadbourne adequately warned them of the potential risk of using the SP Structure, and the Russian authorities, no matter what initially brought them to plaintiffs' doorstep, would have had no basis for continuing their investigation into plaintiffs' business.

could embarrass such other proceedings if I were to seek to determine issues over which I had no jurisdiction.

¹² Defendant contends that this constitutes a shifting position on the part of plaintiffs, since they have repeatedly asserted in their pleadings (including the Second Amended Complaint) and in prior briefs that the SP Structure was illegal and that defendant erroneously concluded that the SP Structure was consistent with Russian law.

However, plaintiffs have offered no admissible evidence in support of their claim that the SP Structure fueled the Tax Police investigation. Therefore, this Court finds that plaintiffs' claim that the SP Structure impacted the length and scope of the investigation "is purely speculative and cannot support a legal malpractice claim." *Ambase v Davis Polk & Wardwell*, 8 NY3d 428, 436 (2007).

A different result would not be reached even were this Court to have granted motion sequence number 024 and considered the resolution dated February 28, 2000 of the Tax Police Investigator, which addresses a possible violation of Decree No. 529. That document is insufficient by itself to raise an issue of fact and plaintiffs have agreed pursuant to Stipulation dated June 27, 2007 that they will not

offer in this action the Testimony of any fact witness who is a present or former official of any agency, instrumentality or organ of the government of the Russian Federation (a 'Russian Government Witness') regarding facts related to plaintiffs' Russian operations that the Russian Government Witness learned in the course of his or her official duties, unless the Russian Government Witness has, as of the close of fact discovery, already given deposition testimony in this action.¹³

¹³ Inspector Dubov was never deposed in this action, which is now pending on the trial calendar.

Accordingly, based on the papers submitted and the oral argument held on the record on December 12, 2008, this Court finds that plaintiffs cannot demonstrate that they would not have sustained their claimed damages, including the loss of their business in the Russian Federation, "but for" Chadbourne's alleged negligence.

Therefore, the defendant's motion for summary judgment must be granted. The Clerk may enter judgment dismissing the Second Amended Complaint with prejudice and without costs or disbursements.

This constitutes the decision and order of this Court.

Dated: January 8, 2010



BARBARA R. KAPNICK
J.S.C.

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