Winter is Coming: The Expanding Definition of Assets in Freezing Injunctions

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In the recent case of *JSC BTA Bank* v *Ablyazov* [2015] UKSC 64, the UK Supreme Court has given important guidance on the scope of the standard form of freezing order issued by the English courts.

Background

Muktar Ablyazov was once a member of the political elite in Kazakhstan and a protégé of its president, Nursultan Nazarbayev. In 1998 he was appointed to the coveted post of Minister of Energy, Industry and Trade. He used his position of influence to secure favourable business deals, including the acquisition of shares in Bank TuranAlem, which later came to be known as BTA Bank ("BTA").

In late 2001, Ablyazov broke ranks with Nazarbayev's ruling party, citing disenchantment with corruption in the president's inner circle. He co-founded an opposition movement, Democratic Choice of Kazakhstan, to challenge the Nazarbayev regime. It was not long before Ablyazov was arrested. The charge was 'abusing official powers as a minister'. Unsurprisingly, the arrest was deemed by Amnesty International and the European Parliament to be 'politically motivated'.

Ablyazov was convicted and sentenced to six years in prison, where he alleged that he was subjected to regular beatings and torture, but was released after only ten months on the condition that he renounce politics. On his release from prison, however, Ablyazov continued to fund independent media and political groups opposed to Nazarbayev. He used his new-found freedom to re-establish ties with BTA, and in 2005 became its chairman. He held this position until early 2009, when BTA executives accused him of illicitly transferring vast sums of money from the bank to companies beneficially owned by him. Kazakhstan's sovereign wealth fund, Samruk-Kazyna, subsequently injected significant funds into BTA and became the majority shareholder, effectively nationalising the bank. Ablyazov claimed that the allegations and the state's takeover of BTA were all part of Nazarbayev's plan to ruin him by any means possible.

Fearing being put on trial again in Kazakhstan, Ablyazov fled to England, where he had substantial assets, including a property in North London on The Bishop's Avenue (known as "Billionaire's Row"), and a 100 acre country estate in Surrey. In March 2009, BTA commenced proceedings in the English High Court to recover the assets Ablyazov had allegedly misappropriated. This marked the beginning of what one judge described as "extraordinary litigation on a huge scale", consisting of dozens of claims and counterclaims between Ablyazov and BTA.

One of the earliest applications made by BTA was for a worldwide freezing order ("WFO") over Mr Ablyazov's assets. BTA argued that there was a real risk that Ablyazov would dissipate his assets before any judgment in their favour could be enforced. Mr Justice Blair agreed with BTA and, in August 2009, ordered a WFO in the following terms:

"4. Until judgment or further order … the respondent must not, except with the prior written consent of the Bank's solicitors –

a. Remove from England and Wales any of his assets which are in England and Wales … up to the value of £451,130,000 …

b. In any way dispose of, deal with or diminish the value of any of his assets in England and Wales up to the value of … £451,130,000 …

c. In any way dispose of, deal with or diminish the value of any of his assets outside England and Wales unless the total unencumbered value … of all his assets in England and Wales … exceeds £451,130,000 …

5. Paragraph 4 applies to all the respondents' assets whether or not they are in their own name and whether they are solely or jointly owned and whether or not the respondent asserts a beneficial interest in them. For the purpose of this Order the respondents' assets include any asset which they have power, directly or indirectly, to dispose of, or deal with as if it were their own. The respondents are to be regarded as having such power if a third party holds or controls the assets in accordance with theirdirect or indirect instructions."

The WFO contained a standard exception to these terms, namely that Ablyazov was permitted to spend a reasonable amount on legal representation and a fixed amount on "ordinary living expenses". It is some indication of Ablyazov's wealth that the court deemed his ordinary living expenses to be £10,000 per week.

Shortly after the WFO was issued, Ablyazov entered into two loan facility agreements with a BVI company called Wintrop Services Limited ("Wintrop") and a further two agreements, in materially the same terms, with another BVI company called Fitcherly Holdings Limited ("Fitcherly"), (collectively, "the Loan Agreements"). Each of the Loan Agreements provided for a facility of £10 million to be made available to Ablyazov. The terms of the Loan Agreements were highly favourable to Ablyazov: he was not required to provide security for the loans (which would be 'dealing' with his assets within the meaning of the WFO) and the lenders were not entitled to demand repayment until four years after the commencement of the facility.

Ablyazov subsequently drew down the full amount of £40 million allowed by the Loan Agreements, directing that Wintrop and Fitcherly make the payments directly to various third parties. The majority of the money was used to fund Ablyazov's gargantuan legal bill. Payments were made to over ten leading counsel, more than 20 juniors and to 75 other lawyers from at least eight different firms. Over £10 million was paid to one firm of solicitors alone: Christmas had certainly come early. Smaller amounts (relatively speaking) were also used to pay various personal expenses, such as approximately £350,000 in connection with Ablyazov's property on The Bishop's Avenue.

In 2012, BTA brought proceedings in the High Court seeking a declaration that Ablyazov's rights under the Loan Agreements were "assets" within the meaning of the WFO. It would follow that Ablyazov had breached the WFO by spending more than a reasonable amount on legal representation and more than £10,000 per week on living expenses. BTA also sought disclosure of all drawings made pursuant to the Loan Agreements to enable it to trace, and if possible recover, the proceeds.

BTA's primary position was that the Loan Agreements were a sham and that Ablyazov was in ultimate control of both Wintrop and Fitcherly. Mr Justice Clarke, in related proceedings between BTA and Ablyazov, said that there was good reason to suppose that this was the case, but declined to decide the point on the basis that it had not been fully argued before him. Ablyazov maintained that the loans were made to him by trusted friends and associates in control of Wintrop and Fitcherly. In any event, BTA was prepared to accept for the purpose of the proceedings that the Loan Agreements were validly entered into at arm's length between commercial parties.

The Parties' Arguments

BTA put forward two arguments explaining why Mr Ablyazov's rights under the Loan Agreements were assets within the meaning of the WFO. Its primary argument was that a right to borrow money from a lender under a loan facility is a 'chose in action' (a property right in something intangible) and English law has long classified choses in action as assets. BTA's secondary argument was that, if a right to borrow money is not usually classified as an asset in the context of a freezing order, the extended definition of asset in paragraph 5 of the WTO was broad enough to cover Ablyazov's rights under the Loan Agreements. In either case, Ablyazov had 'dealt' with that asset by directing payments pursuant to the Loan Agreements to third parties.

BTA argued that if the position were otherwise, a defendant subject to a WFO could borrow a large sum of money, thereby reducing his overall net asset position by that amount, and potentially reducing the amount available for the claimant by the full extent of the loan if, say, the lender obtained a judgment for that amount before the claimant's claim was established. The defendant would therefore in effect be allowed to make payments out of his assets without regard to the restrictions

imposed on him by the WFO.

Ablyazov's counter argument rested on direct legal authority. Neuberger J, as he then was, in *Cantor Index Ltd v Lister [2002]* CP Rep 25, held that a defendant who borrows money increases his indebtedness but does not dispose of, deal with or diminish the value of his assets within the meaning of a freezing order. In response to the argument that this approach would allow a defendant to in effect circumvent a freezing order by reducing his net asset position, Neuberger J said the following (emphasis in original):

"I see the force of that submission as a matter of good sense and practicality. However I do not think that it is right, in light of the words of paragraphs 1(1) and 1(2) of the order. They provide that the defendant should not "dispose of, deal with or diminish the value of any of his assets". For a debtor to increase his indebtedness by borrowing from an existing creditor or even to create an indebtedness by borrowing from a new creditor, at least where the creditor is not secured on any of the debtor's assets, does not to my mind, as a matter of ordinary language, involve disposing of or dealing with or diminishing the value of any of the debtor's assets . I accept that it results in a diminution of the debtor's net asset position, but that is not what paragraphs 1(1) and 1(2) of the Freezing Order refer to."

BTA submitted that *Cantor Index* could be distinguished on the facts because the freezing order Neuberger J was referring to did not contain the extended definition of 'assets' present in paragraph 5 of the WFO. The definition, it was argued, was wide enough to cover an intangible right which, if exercised, which would indirectly diminish the value of a debtor's assets.

Ablyazov submitted that the new wording made no difference to the position as it was under *Cantor Index*. The expanded definition was directed at a different situation, namely where the asset in question is held by a third party in circumstances where the respondent has the power to control the asset but may hold something short of a legal or beneficial title (e.g. because he is a trustee or nominee of the asset). Ablyazov argued that the expanded definition was aimed at clarifying what *type* of interest the respondent must have in the property rather than the *nature* of the assets in which an interest may be had for the purposes of the freezing order. A right to borrow money under a loan facility was not an asset within the meaning of the WFO because it was not something that could be diminished in value.

Decision of the High Court

The judge, at first instance, agreed with Ablyazov. He held that the right to borrow money was not to be regarded as an 'asset' within the meaning of the WFO. The purpose of the WFO was to prevent Ablyazov from disposing of his assets so as to frustrate an attempt by BTA to enforce any future judgment it might secure against him. It followed that the assets to which the WFO referred are assets which could be of some value to BTA and against which BTA would be capable of securing execution.

The judge found the rights to borrow under the Loan Agreements had no monetary value that BTA could realise. There was no secondary market for such rights. The loan facility was non-assignable, and the lenders would have no incentive to agree to transfer the rights by novation to BTA on the same favourable terms as the original lending facility. Because Ablyazov's rights had no value to BTA, it could not have been intended that the exercise of those rights should be subject to the WFO.

The judge held that the extended definition of assets in the WFO did not change this position. Ablyazov did not deal with any asset as if it was his own. He could only exercise his right to direct money to be paid under the loan facility. Until the money reached the payees, the lenders owned and controlled that asset and they alone had the power to deal with it as their own. For these reasons, BTA's application was dismissed.

Decision of the Court of Appeal

The Court of Appeal upheld the first instance decision. The leading judgment was given by Beatson LJ, whose judgment focused on three principles that he held were relevant to the construction of a freezing order.

The first, and most important, of these was the 'enforcement principle', which he expressed as follows:

"the purpose of a freezing order is to stop the injuncted defendant dissipating or disposing of property which could be the subject of enforcement if the claimant goes on to win the case it has brought, and not to give the claimant security for his claim".

The second was the 'flexibility principle', namely:

"the jurisdiction to make a freezing order should be exercised in a flexible and adaptable manner so as to be able to deal with new situations and new ways used by sophisticated and wily operators to make themselves immune to the courts' orders or deliberately to thwart the effective enforcement of those orders"

The third was the 'strict construction principle':

"because of the penal consequences of breaching a freezing order and the need of the defendant to know where he, she or it stands, such orders should be clear and unequivocal, and should be strictly construed"

Beatson LJ held that there was a tension between the application of these principles to the interpretation of any freezing order. The first two principles weigh in favour of a broad, purposive interpretation of freezing orders to prevent unscrupulous defendants from creatively evading their intended application. On the other hand, the third principle weighs in favour of a narrow, literal construction because of the potentially draconian effect of a freezing order on the economic freedom of an individual against whom no judgment has yet been granted.

In applying these principles to the WFO over Ablyazov's assets, Beatson LJ reiterated many of the points raised by the judge at first instance. In particular, he emphasised that fact that the rights under the Loan Agreements had no value to BTA and therefore the enforcement principle could not support their construction of the WFO. In summary he held that, applying the strict construction principle, the words of the order were not clear enough to bring the rights under the Loan Agreement within the remit of the WFO. Additional words would need to be added to the standard form freezing order for such rights to be deemed 'assets'.

Neither did the expanded definition of assets in paragraph 5 of the WFO assist BTA. Beatson LJ agreed with Ablyazov that the purpose of the expanded definition was to cover assets that were not beneficially or legally owned by a defendant but over which he had control, for example in his capacity as a trustee or nominee. The control a trustee or nominee has over an asset is very different from the control that Ablyazov had over the money borrowed under the Loan Agreements. A strict construction did not permit a wider interpretation of the expanded definition in paragraph 5 in circumstances where that definition was clearly directed at a different category of asset.

Decision of the Supreme Court

In a short, 12 page judgment, the Supreme Court overturned the decisions of the High Court and the Court of Appeal. Lord Clarke, with whom Lords Neuberger, Mance, Kerr and Hodge agreed, began his judgment by noting that BTA had, by this point, obtained a number of judgments against Ablyazov in the English courts, amounting to a total of $4.4 billion. He then set out what he saw as the key issues before the court:

"(1) whether the respondent's right to draw down under certain loan agreements is an "asset" within the meaning of the Freezing Order;

(2) if so, whether the exercise of that right by directing the lender to pay the sum to a third party constitutes "disposing of" or "dealing with" or "diminishing the value" of an "asset"; and

(3) whether the proceeds of the loan agreements were "assets" within the meaning of the extended definition in paragraph 5 of the Freezing Order on the basis that the respondent had power "directly or indirectly to dispose of, or deal with [the proceeds] as if they were his own."

All of these issues were questions of construction of the WFO. The sole question was what the WFO meant. It followed that the Court of Appeal had been wrong to have regard to the 'flexibility principle' in its analysis. The flexibility principle was concerned only with the court's jurisdiction to make a new freezing order. Lord Clarke agreed that the courts should be "*agile in this game of cat and mouse between claimants and defendants to make sure that it is making new orders to meet new avoidance measures"* but that was not a justification for expansively interpreting an order which had already been made.

The first and second issues of construction related to the standard form of freezing order, which did not contain the extended definition of assets as appeared in paragraph 5 of the WFO. Lord Clarke referred to *Cantor Index* as authority for the proposition that rights to borrow money were not assets under that form of order. It was also authority for the proposition that exercising a right was not 'dealing' with an asset within the meaning of that standard form.

Lord Clarke stressed the importance of clarity and certainty in the interpretation of penal orders. The courts should be slow to depart from an interpretation that has stood for many years. The prudent course for the Supreme Court was to interpret the normal standard form freezing order consistently with the previous understanding of the courts, legal writers and the legal profession.

The same reasoning did not apply to the most recent standard form of freezing order, which included an extended definition of assets in paragraph 5 (set out here again for convenience):

"5. Paragraph 4 applies to all the respondents' assets whether or not they are in their own name and whether they are solely or jointly owned and whether or not the respondent asserts a beneficial interest in them. For the purpose of this Order the respondents' assets include any asset which they have power, directly or indirectly, to dispose of, or deal with as if it were their own. The respondents are to be regarded as having such power if a third party holds or controls the assets in accordance with theirdirect or indirect instructions."

Lord Clarke held that the rights under the Loan Agreements were assets within the meaning of this paragraph. An instruction to a lender to pay the lender's money to a third party is dealing with the lender's assets as if they were his own. That was the natural reading of the second sentence of paragraph 5. The relevant question was whether Ablyazov had the power to direct the lenders what to do with the funds that they were contractually obliged to make available to him. The court found that he did have that power, and so the rights were assets caught by the WFO.

Lord Clarke dismissed the objections to this interpretation of the WFO that had been given by the courts below. In particular, he rejected the contention that paragraph 5 was primarily designed to catch assets that a defendant claims he holds on trust or as a nominee. That was only the aim of the first sentence. By contrast, the last two sentences of paragraph 5 have no specific target, but are simply designed to catch assets which are not owned legally or beneficially, but over which the defendant has control. Lord Clarke clarified that the third sentence of the definition was not a restriction on the scope of the second sentence, but was expansionary.

Comment

The decision of the Supreme Court is welcome news for creditors concerned about an individual indirectly reducing their net asset position by using unsecured borrowing or credit facilities. Any application for a freezing order (whether in English court proceedings or in an application ancillary to an English law arbitration) should seek to include the extended definition of assets in the order as a matter of course. The effect of this is that it will no longer be possible for a defendant to indirectly circumvent the standard exceptions to a freezing order by using borrowing or credit facilities, without facing the serious consequences that a breach of a court order entails.

The decision may also have implications for the question of whether a freezing order made against a sole shareholder and director of a company extends so as to cover that company's assets. In the case of *Lakatamia Shipping* v *Su* [2015] 1 WLR 291, the Court of Appeal said that in those circumstances the company's assets were not covered by the extended definition of assets in the new standard form freezing order. The reason given was that the paragraph 5 "*was not intended to include*

the assets of another person". The Supreme Court has now held the opposite. The extended definition may catch the assets of another person if they are in the control of the defendant. It remains to be seen whether the courts will attempt to distinguish this set of circumstances or follow through with the logical consequence of the Supreme Court's reasoning.

Conclusion

It is fitting to conclude by telling the remainder of Abylazov's story. By the time the Supreme Court was delivering its judgment in October 2015, Abylazov's concerns were much bigger. In February 2012 he had been found guilty of three deliberate and substantial contempts of court for failing to disclose the location of assets he had fraudulently misappropriated from BTA. Maurice Kay LJ, sitting in the Court of Appeal in the contempt proceedings went so far as to say:

"*It is difficult to imagine a party to commercial litigation who has acted with more cynicism, opportunism and deviousness towards court orders than Mr Ablyazov*"

Ablyazov was given three consecutive 22 month prison sentences. Just before the sentencing hearing, however, Ablyazov fled the country and went into hiding. He was eventually tracked down in July 2013, by private investigators working for BTA, when they followed one of Abylazov's associates from the High Court in London to Heathrow airport, and onto a villa in the south of France. Ablyazov was subsequently arrested by the French police in a dramatic dawn raid. He is now awaiting extradition to Russia to face a long list of charges for embezzlement and fraud.

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