

MOSCOW CORPORATE CRIME AND INVESTIGATIONS NEWSLETTER - JANUARY 2020

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Legal Briefings

This newsletter summarises recent developments in Russian regulations, enforcement and court practice which may be relevant for doing business in Russia, from a corporate crime and investigations perspective.

Additionally, this newsletter identifies some developments in the US and other relevant jurisdictions which should be kept in mind by Russian businesses having foreign parent companies or operations.

RECENT REGULATORY DEVELOPMENTS

Criminal Code developments

In late December 2019, the President of the Russian Federation filed with the State Duma, the lower chamber of the Russian Parliament, a bill effectively making it impossible to charge an individual with the crime of organising a criminal community (an "OCC Charge") in the context of economic crimes.

In the last few years, and in 2018-19 especially, we have noted a very important trend in enforcement related to the use of OCC Charges. The criminal investigation authorities have launched a number of high-profile criminal cases where businessmen have faced an OCC Charge in addition to being charged with having committed commercial fraud and other business-related crimes.

The organisation of a criminal community is a serious crime, generally punishable by up to 20 years of imprisonment (or even by life imprisonment in limited cases). Supreme Court practice indicates that a criminal community is defined as a structured, hierarchal organisation designed with the aim of committing serious criminal activities.

Historically, OCC Charges were used in the 1990s to combat the massive rise in organised violent crime which took place after the fall of the Soviet Union.

However, recently, the investigative authorities have started charging the managers and beneficiaries of various large scale businesses with organising criminal communities based on allegations that those businesses have been involved in various serious crimes such as tax evasion or fraud. This is problematic because any legal entity or holding structure inevitably fits with the "structured, hierarchical organisation" definition of an organised criminal community given by the Supreme Court (including by meeting the definition's requirements in respect of the organisation's delegation of powers, split of functions etc.), meaning that if some of an organisation's managers or employees have committed (or are alleged to have committed) a crime, the authorities often claim that the entire organisation was designed for that purpose.

Apart from being used as leverage in corporate conflicts, an OCC Charge allows the investigating authorities to circumvent the prohibition on the pre-trial detainment of businessmen facing charges connected with business-related crimes, as the organisation of a criminal community does not fall within the definition of a business-related crime.

The fact that the bill has been introduced by the President indicates that the government is aware of the issues with the enforcement of the legal regime relating to the organisation of criminal communities and is aiming to improve the business climate in Russia. The bill appears to have a fair chance of being adopted. However, we are sceptical of the notion that - if it is adopted - the bill will quickly change the trends identified above: earlier procedural amendments banning the pre-trial detainment of individuals charged with business-related crimes have remained virtually unenforced for several years now.

Statistics

According to statistics compiled in relation to anti-corruption laws, during the first half of the year 2019:

- 140,379 violations of anti-corruption laws were detected;
- 1,858 criminal cases were initiated;
- 4,146 offenders were punished under administrative laws; and
- 187 legal entities were held administratively liable for breaches.

COURT PRACTICE AND ENFORCEMENT DEVELOPMENTS

In October 2019, the Constitutional Court handed down its ruling in the notorious Zakharchenko case. This case related to various corruption allegations made against Mr. Zakharchenko, and resulted in over 8 billion roubles in cash and several dozen real estate assets being confiscated from Mr. Zakharchenko and his associates.

The Constitutional Court specifically considered an application made by several individuals who claimed that various real estate assets were confiscated from them on the false grounds that they held these assets on trust for Mr. Zakharchenko. The applicants claimed that, while confiscation of property is possible in relation to state officials who are obliged to report their income and spending but who fail to prove the legality of the source of the income used to acquire that property, the applicants did not fall within the category of being such state officials and were neither obliged to report their income or their spending, and that therefore they should be exempt from the confiscation of their property.

The Constitutional Court concluded that the confiscation of property by a court is possible if two conditions are simultaneously met:

- (i) it is proven that the property in question was acquired using the income of a corrupt official; and
- (ii) the legal owner of the property in question cannot prove the legal sources of his own income used to fund the acquisition of the property.

The Court noted that the owner of such property can present any possible proof of the legality of the sources of income from which the acquisition was financed. In cases where the property owner confirms the legality of such income sources, such property cannot be seized.

This approach appears measured and does not extend the confiscation regime applicable to state officials to their associates or families automatically. However, if in the course of the prosecution of a corrupt state official the court proves that the official channelled illegal funds to third parties, such third parties would then be subject to the confiscation regime.

At the same time, the application of the Constitutional Court's position by the criminal prosecution authorities may raise issues. Statistics indicate that only 0.25% of all judgements in Russian criminal cases are acquittals. Therefore, if the prosecuting authorities bring a corruption case against a state official to court, and allege that the acquisition of certain property by third parties was financed by illegal funds owned by the state official being prosecuted, the allegation would most likely be approved by a court and would cause inevitable confiscation problems to such third parties.

The takeaway for Russian businesses is that it is advisable to limit, to the extent possible, business operations with state officials (or those officials' family members or close friends) in order to limit exposure to the confiscation regime set out above.

FOREIGN DEVELOPMENTS AND ENFORCEMENT NEWS

European Union ("EU")

In November 2019, the draft form of Directive (EU) 2019/1937 on the protection of persons who report breaches of EU law (the Whistleblowing Directive) was published in the Official Journal of the EU.

The Whistleblowing Directive was proposed with the aim of establishing safe internal and external channels of reporting for whistleblowers within a variety of different organisations. Under the directive, both private and public organisations must provide safe channels for whistleblowers to make reports, following which those individuals will be protected against any retaliation. The directive also introduces an obligation for national authorities to adequately inform citizens and public officials on how to deal with whistleblowing.

Foreign Corrupt Practices Act of 1977 ("FCPA") enforcement

In August 2019, the Securities and Exchange Commission announced that Deutsche Bank AG ("**Deutsche Bank**") will pay more than \$16 million to settle charges that it violated the FCPA by hiring relatives of foreign government officials in the Asia-Pacific region and in Russia in order to influence those officials in connection with Deutsche Bank's investment banking business.

These "referral hires" bypassed Deutsche Bank's highly competitive and merit-based hiring process and resulted in the employment of often less qualified individuals than those applicants hired through the bank's formal hiring process. Without admitting or denying the findings, Deutsche Bank agreed to pay the \$16 million settlement figure.

Violation of sanctions regulations

Apple Inc. ("**Apple**") will pay nearly US \$467,000 to the US Treasury Department for hosting a sanctioned Slovenian software developer on its platform. SIS d.o.o. and its owner Savo Stjepanovic were placed on a sanctions list over suspected ties to a steroid trafficking ring, but Apple hosted the company's software on its App Store and processed nearly 50 payments to the company between 2015 and 2017.

The US Treasury Department said that the lapse, which resulted in Apple processing a total of US \$1.15m in App Store payments to SIS, was an apparent violation of the agency's Foreign Narcotics Kingpin Sanctions Regulations.

Apple noticed the oversight after enhancing its compliance software in 2017 and immediately suspended further payments to SIS, according to the enforcement notice. The company agreed to upgrade its screening tools to catch spelling and capitalisation quirks and widen the range of people it screens in respect of sanctions as part of its deal with regulators.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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