



# **REIDERSTVO 2.0:**

THE ILLEGAL RAIDING PANDEMIC IN RUSSIA

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## SUMMARY

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- The current trend that became more obvious over the last five years can be characterized as a pandemic of illegal raiding, with cases spreading across all Russia's regions undermining their socioeconomic development and destroying their investment climate.
- A rising number of cases involve malicious criminal prosecution of entrepreneurs whose assets became subject to economic disputes and were targeted by private and public raiders with strong connections to law enforcement agencies.
- Mistrust in law enforcement and courts continues to grow in Russia, with the vast majority of entrepreneurs believing that the justice system is neither independent nor objective.
- Entrepreneurship is considered one of the most dangerous occupations in Russia, with the vast majority of entrepreneurs saying it is unsafe to do business in the country.
- The country's leadership is well aware of the damage being inflicted on Russia's business climate, but in many cases, they are either the beneficiaries of or active participants in illegal raiding.
- Raids against the assets of well-known Western investors in Russia have contributed to the hesitancy of foreign investors to do business in Russia.
- Illicit financial gains from raiding are laundered into the international financial system, and this inflow of dirty money contributes to the corrosion of financial and political institutions of the recipient countries.
- There is growing evidence that corrupt officials, law enforcement, and illegal raiders from Russia misuse the international police organization Interpol, legal procedures in Western courts and arbitration bodies, the media, and the globalized financial system to their advantage.
- Since raiding cases have increasingly gone to foreign courts and arbitration bodies for litigation, it is important that Western experts learn how to identify the "red flags" of a raiding case.

<sup>6</sup>U.S. Senate (2018) *Report of the Select Committee on Intelligence on Russian Active Measures Campaigns and Interference in the 2016 U.S. Election*, [https://www.intelligence.senate.gov/sites/default/files/documents/report\\_volume5.pdf](https://www.intelligence.senate.gov/sites/default/files/documents/report_volume5.pdf), accessed February 10, 2021.

<sup>7</sup>Marandici, I. (2021) "Taming the Oligarchs? Democratization and State Capture: The Case of Moldova," *Demokratizatsiya*, 29(1), 63–89; Derevyanko, B. et al. (2020) "Addressing the Issue of Corporate Raiding in Ukraine," *Problems and Perspectives in Management*, 18(1), 171–80; Lewis, D. and Sagnayeva S. (2020) "Corruption, Patronage and Illiberal Peace: Forging Political Settlement in Post-Conflict Kyrgyzstan," *Third World Quarterly*, 41(1), 77–95; Viktorov, I. (2019) *Russia's Network State and Reiderstvo Practices*, in B. Magyar (ed.), *Stubborn Structures: Reconceptualizing Post-communist Regimes* (pp. 437–459), Budapest: CEU Press.

<sup>8</sup>Madlovics, B., and Magyar B. (2021) *The Anatomy of Post-Communist Regimes: A Conceptual Framework*, Budapest–New York: CEU Press, <https://library.oapen.org/handle/20.500.12657/46598>, accessed March 7, 2021.

# INTRODUCTION

The original report “*The Rise of Reiderstvo: Implications for Russia and the West*” was published in 2016. Five years have passed, but there has been no improvement in the Russian business environment since then. Over the last years, there has been a substantial rise in the number of illegal raiding cases, particularly those involving malicious criminal prosecution against businessmen targeted by raiders. This illegal raiding pandemic is having devastating effects on Russian businesses, already weakened by financial and social disruption caused by COVID-19 restrictions and lockdowns. Moreover, even the most prominent foreign investors doing business in Russia are not protected from malicious criminal prosecution initiated by private or public raiders.

The impact of reiderstvo on Western economies and democratic institutions requires special attention. Until the Magnitsky case, illegal business raiding in Russia was seen by the outside world primarily as Russia’s domestic issue. Yet, now there is a widely-shared consensus that reiderstvo should be a much higher priority for other countries, given its impact on today’s increasingly globalized world. Since 2016,

there has been a growing interest in research on the damage it causes to international financial and political institutions. Exploitative and manipulative practices of officials, raiders, and criminals from Russia and other authoritarian countries are well documented in the areas of the misuse of the international police organization *Interpol*,<sup>1</sup> legal procedures in Western courts and arbitration bodies,<sup>2</sup> the media,<sup>3</sup> and the globalized financial system.<sup>4</sup> Building on the previous research, this report provides an analysis of new trends in reiderstvo, the most common methods and tactics in recent raiding cases, and their connections with corruption and other types of criminal activities in Russia.

Western efforts to punish Russian public officials engaged in illegal business raiding, corruption, and human rights violations have grown in recent years, but these illegal activities have increased far more.<sup>5</sup> The Sergei Magnitsky Rule of Law Accountability Act of 2012 (also known as the Magnitsky Act) and the subsequent Global Magnitsky Human Rights Accountability Act of 2016 (the Global Magnitsky Act) proved effective in targeting some of the high-ranking officials by freezing their property and

banning them from entering the United States. The success of these acts is evident in vigorous efforts undertaken by Russian political circles to prevent their adoption.<sup>6</sup> In this context, it is important to raise awareness among policymakers, public officials, private companies, investors, and the general public of the dangers associated with illegal business raiding in Russia for the national economy and Western democracies.

This report focuses on Russia; yet, its analysis can be applied to many post-communist countries. The spread of the “reiderstvo virus” in other post-communist countries has been recently well documented in Moldova, Ukraine, Kyrgyzstan, and some other Central Asian republics.<sup>7</sup> The list of predatory states also includes one member of the European Union – Hungary, with its modified variant of reiderstvo characterized by less obvious and more sophisticated methods of asset seizures.<sup>8</sup> These countries share similar characteristics, including systematic and centralized corruption, abuse of the legislative, judicial, and enforcement systems, and the use of state violence to take over economic resources.

<sup>1</sup> TraCCC (2018) *Spotlight on a Critical Threat: The Abuse and Exploitation of Red Notices, Interpol and the U.S. Judicial Process by Russia and Other Authoritarian States*, <https://tracc.gmu.edu/sites/default/files/TraCCC/Final-Red-Notices-Conference-Report-Bright-Red.pdf>, accessed February 10, 2021; Fair Trials International (2018) *Dismantling the Tools of Oppression: Ending the Misuse of Interpol*, London: Fair Trials International.

<sup>2</sup> Åslund, A. (2018) *Russia’s Interference in the US Judiciary*, Washington, D.C.: Atlantic Council; Free Russia Foundation (2019) *Misrule of Law: How the Kremlin Uses Western Institutions to Undermine the West*, Washington, D.C.: Free Russia Foundation.

<sup>3</sup> Foxall, A. (2020) *Russian ‘Black PR’: Examining the Practice of Ruining Reputations*, London: Henry Jackson Society.

<sup>4</sup> TraCCC (2018) *Money Laundering in Real Estate*, [https://tracc.gmu.edu/sites/default/files/2018-MLRE-Report\\_0.pdf](https://tracc.gmu.edu/sites/default/files/2018-MLRE-Report_0.pdf), accessed February 10, 2021; TraCCC (2019) *Trade Based Money Laundering*, <https://tracc.gmu.edu/sites/default/files/TBML%20Conference%20Report.pdf>, accessed February 9, 2021; Transparency International (2016) *Paradise Lost*, London: TI; Transparency International (2021) *Safe Haven*, Dublin: TI.

<sup>5</sup> Lain, S. (2017) “Russia’s Corporate Raiders Add to Threat from Sanctions,” *Financial Times*, August 17; Lain, S. (2017) *Corporate Raiding in Russia: Tackling the Legal, Semi-Legal and Illegal Practices that Constitute Reiderstvo Tactics*, London: RUSI.

<sup>6</sup> U.S. Senate (2018) *Report of the Select Committee on Intelligence on Russian Active Measures Campaigns and Interference in the 2016 U.S. Election*, [https://www.intelligence.senate.gov/sites/default/files/documents/report\\_volume5.pdf](https://www.intelligence.senate.gov/sites/default/files/documents/report_volume5.pdf), accessed February 10, 2021.

<sup>7</sup> Marandici, I. (2021) “Taming the Oligarchs? Democratization and State Capture: The Case of Moldova,” *Demokratizatsiya*, 29(1), 63–89; Derevyanko, B. et al. (2020) “Addressing the Issue of Corporate Raiding in Ukraine,” *Problems and Perspectives in Management*, 18(1), 171–80; Lewis, D. and Sagnayeva S. (2020) “Corruption, Patronage and Illiberal Peace: Forging Political Settlement in Post-Conflict Kyrgyzstan,” *Third World Quarterly*, 41(1), 77–95; Viktorov, I. (2019) *Russia’s Network State and Reiderstvo Practices*, in B. Magyar (ed.), *Stubborn Structures: Reconceptualizing Post-communist Regimes* (pp. 437–459), Budapest: CEU Press.

<sup>8</sup> Madlovics, B., and Magyar B. (2021) *The Anatomy of Post-Communist Regimes: A Conceptual Framework*, Budapest–New York: CEU Press, <https://library.oapen.org/handle/20.500.12657/46598>, accessed March 7, 2021.

## WHAT ARE THE MOST RECENT TRENDS BASED ON STATISTICS?

**The number of illegal raiding cases in Russia has been growing over the last years, particularly cases involving malicious criminal prosecution against legal business owners.**

*The official statistics from the Investigative Committee of the Russian Federation show that in 2019, the number of illegal business raiding cases in Russia increased by 135% compared to the previous year.<sup>9</sup> In the same year, 317,627 economic crime cases were opened against entrepreneurs (under Articles 159, 160, and 165 of the Criminal Code), representing a 37%-increase over 2018.<sup>10</sup>*

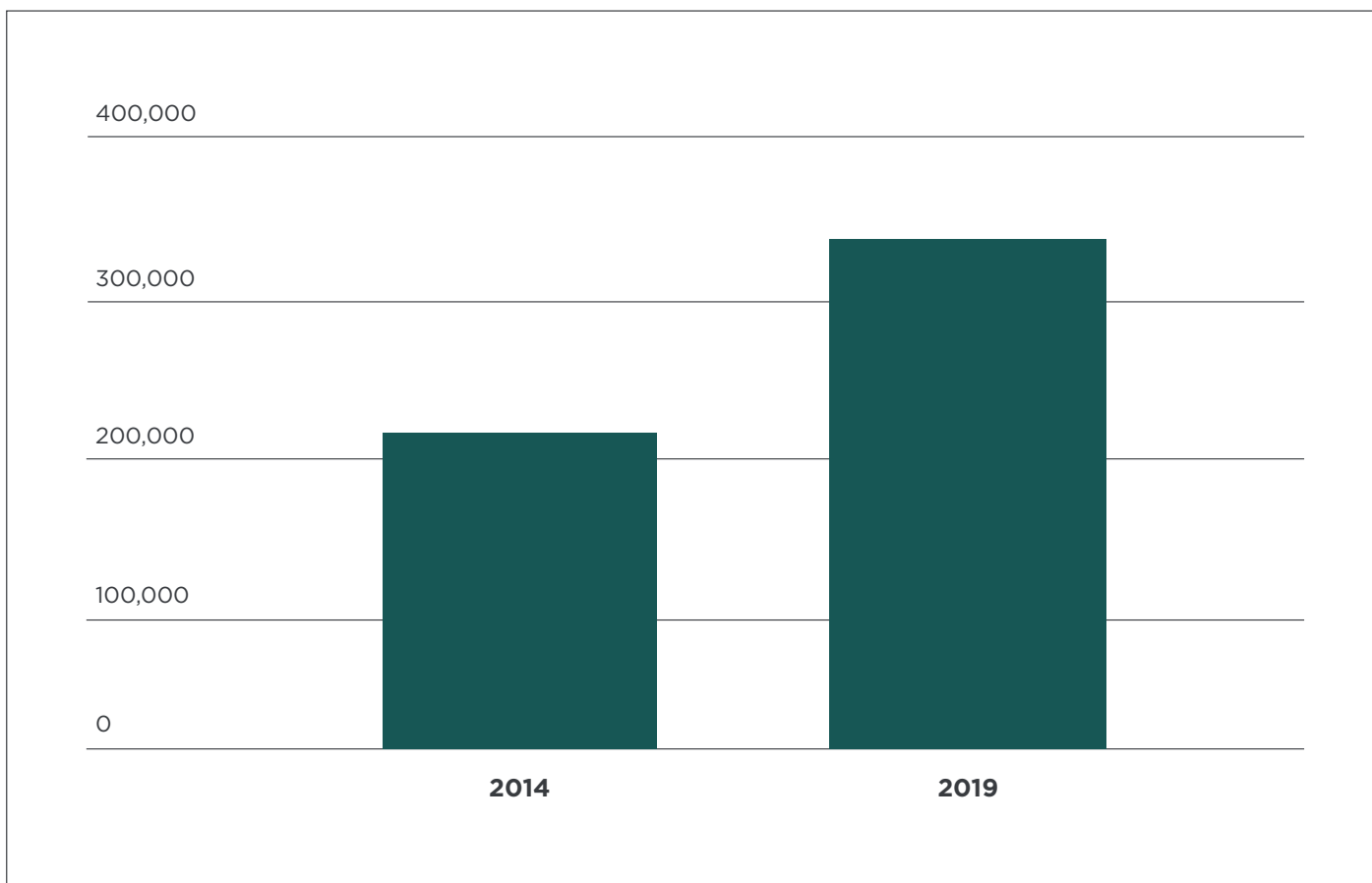
### **AN INCREASE IN ECONOMIC CRIME CASES**

Back in 2015, during his address to the Federal Assembly, President Putin himself noted that investigative authorities had opened nearly 200,000 economic crime cases in 2014. Of those 200,000 economic crime cases, only 15% resulted in a conviction, but a full 83% of businessmen still ended up losing control of their businesses. Even President Putin admitted that these figures suggest that companies were harassed, intimidated, robbed, and released.<sup>11</sup> Comparing the 2014

*and 2019 official statistics points to a 59%-increase in economic crime cases over the five-year period.*

**Although the overall number of criminal cases against entrepreneurs is only an indirect indicator of reiderstvo, it gives some approximation of how many businesses were subject to state pressure.**

**FIGURE 1 : INCREASE IN ECONOMIC CRIME CASES BETWEEN 2014 AND 2019**



<sup>9</sup> "За год число дел о рейдерских захватах в России выросло на 135%" [in Russian] (2020) TASS, March 3, <https://tass.ru/obschestvo/7886589>, accessed February 10, 2021.

<sup>10</sup> Business Ombudsman of the Russian Federation (2019) "Boris Titov zayavil, chto v 2019 godu ugolovnoye presledovaniye v ekonomicheskoy sfere tol'ko usugubilos" [in Russian], <https://ombudsmanbiz.ru/2020/02/boris-titov-zajavil-cto-v-2019-godu-ugolovnoe-presledovanie-v-jekonomicheskoy-sfere-tolko-usugubilos/>, accessed February 12, 2021.

<sup>11</sup> President of Russia (2015) The Presidential Address to the Federal Assembly, <http://en.kremlin.ru/events/president/news/50864>, accessed February 2, 2016.



**REASONS FOR OPENING CRIMINAL CASES AGAINST ENTREPRENEURS**

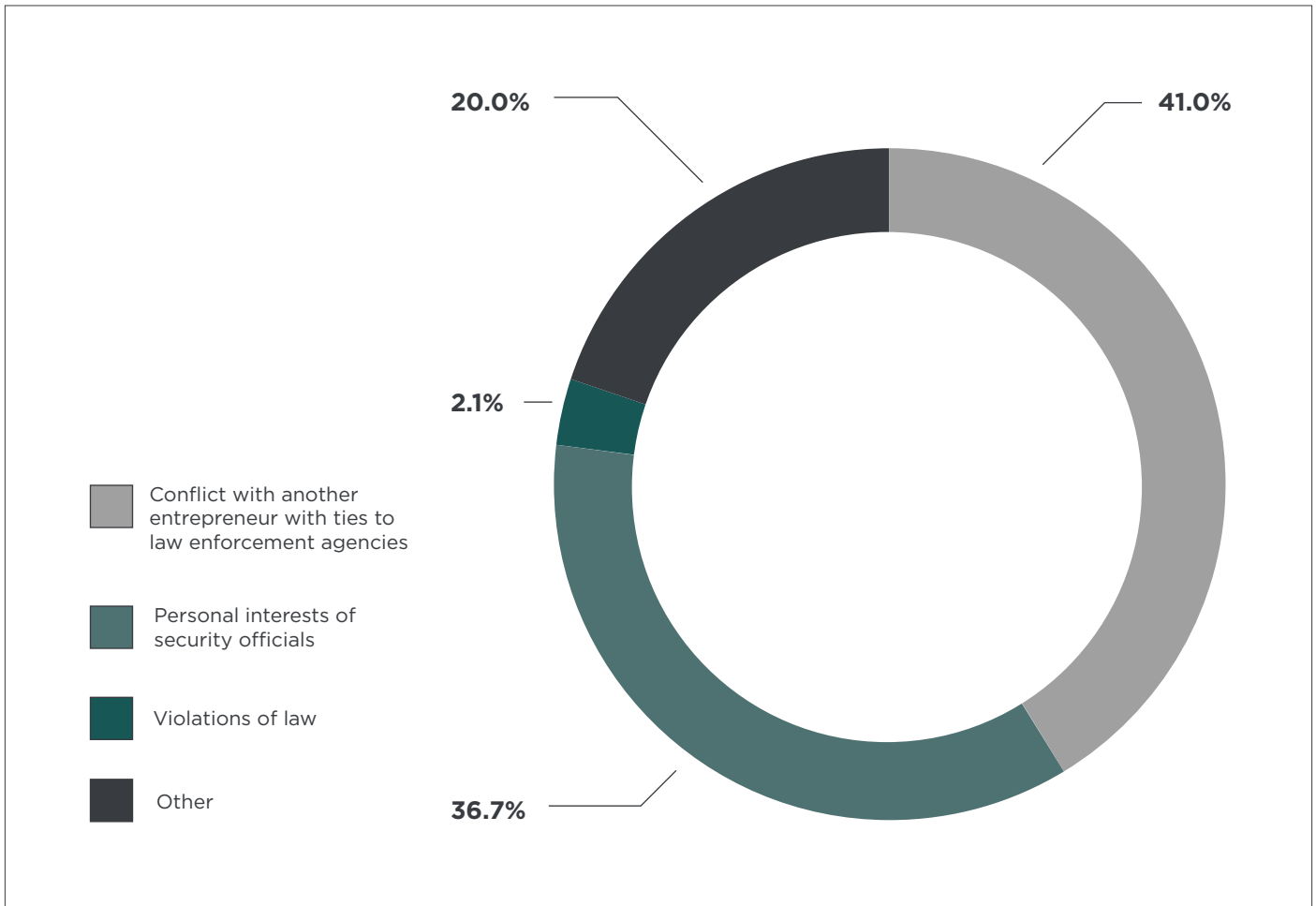
According to the 2019 survey conducted by the Federal Guard Service for the Russian ombudsman, Boris Titov, among 181 experts and 211 criminally prosecuted entrepreneurs, 41% of respondents believed that the reason for initiating a criminal case against them was a conflict with another entrepreneur connected to law enforcement agencies; 36.7% linked it to personal interests of security officials (also called

“siloviki” in Russian); and only 2.1% pointed to violations of the law. As the result of these criminal cases, 84.3% of entrepreneurs reported that they partially or completely lost their businesses, while 64% of them also suffered damage to their health and reputation from the malicious criminal prosecution. The country’s leadership is well aware of this problem. In May 2019, President Putin held a working meeting with Russia’s business ombudsman who presented his annual report on human rights and

entrepreneurship. As for malicious criminal prosecution of businessmen, he cited very alarming statistics: “Over 80% of entrepreneurs consider doing business in the country unsafe, [and] unfortunately, this number is growing.”

“Over 80% of entrepreneurs consider doing business in the country unsafe.”

**FIGURE 2 : COMPLAINTS OF ENTREPRENEURS TO RUSSIA’S BUSINESS OMBUDSMAN**



<sup>12</sup> Ruvinsky, V. (2019) “Zhaloby naverkh i v nikuda” [in Russian], *Vedomosti*, May 29, <https://www.vedomosti.ru/opinion/articles/2019/05/29/802688-zhalobi-naverh>, accessed February 10, 2021.

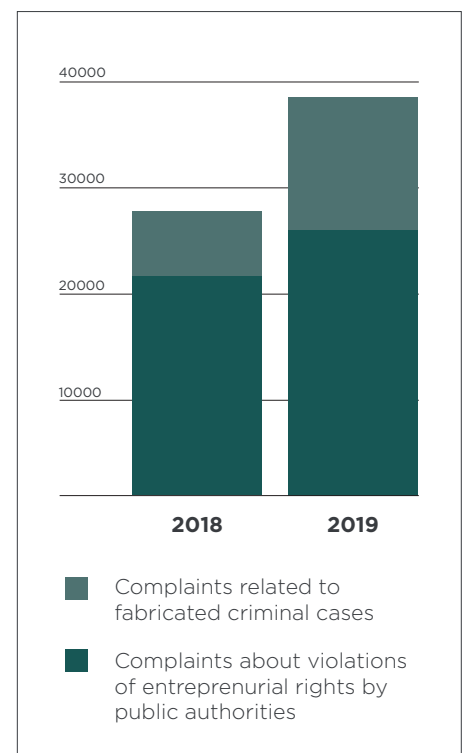
<sup>13</sup> Ibid.  
<sup>14</sup> President of the Russian Federation (2019) “Vstrecha s upolnomochennym po zashchite prav predprinimateley Borisom Titovym” [in Russian], May 27, <http://kremlin.ru/events/president/news/60583>, accessed February 10, 2021.

In 2019, Boris Titov received over 24,000 complaints from entrepreneurs about violations of their rights by Russian authorities, which constituted a 24%-increase compared to 2018. Moreover, in the same period, the number of complaints about bogus criminal cases opened against legal business owners in the interests of private or public raiders increased from less than a third to almost half of the total number of the complaints to Russia's business ombudsman.

The business ombudsman's office is not the only place where entrepreneurs can file their complaints. At the end of 2019, an autonomous non-profit organization, ANO "Platform for working with complaints from entrepreneurs," launched an official electronic portal "ZaBiznes" where entrepreneurs can file complaints about illegal raiding, violations of their rights, or unlawful actions by law enforcement. As of Janu-

ary 2021, the portal registered 1,520 complaints received over the course of just one year. This number can serve as yet another indicator of rising predations on businesses. In comparison, over a five-year period between 2011 and 2016, an electronic platform launched by the Center for Public Procedures "Business Against Corruption" received 1,057 complaints about illegal raiding and violations of entrepreneurial rights by law enforcement. These numbers, however, are only the tip of the iceberg. Many Russian entrepreneurs do not file official complaints because they do not believe that such complaints will receive an adequate response from the authorities. On the contrary, some cases have been documented where complaints against public officials provoked revenge from other public agencies participating in the same corrupt network. This practice is known as "krugovaya poruka" in Russian, meaning "joint responsibility."

**FIGURE 3 : NATURE OF COMPLAINTS**



## HOW DOES LAWLESSNESS FEED REIDERSTVO?

**Mistrust in law enforcement and courts continues to grow in Russia.** Not only does the country's justice system fail to provide sufficient guarantees to protect

businesses from illegal raiding, but in many cases, it is directly responsible for unjustified criminal prosecution of legal business owners. A Federal Guard Service

survey found that in 2019, 70.7% of respondents did not have trust in the Russian judicial system, while 66.7% of them also did not trust law enforcement.<sup>19</sup> Although

<sup>15</sup> "Russian Businesses Lodge Rising Numbers of Official Complaints" (2020) *The Moscow Times*, February 3, <https://www.themoscowtimes.com/2020/02/03/russian-businesses-lodge-rising-numbers-of-official-complaints-a69137>, accessed February 10, 2021.

<sup>16</sup> ANO Platform (2021) Statistics, <https://забизнес.рф/issues>, accessed February 10, 2021, accessed February 1, 2021.

<sup>17</sup> Kazun, A. (2020). "Stopping the Feast in Times of Plague: Fighting Criminal Corporate Raiding in Diverse Russian Regions," *Post-Soviet Affairs* 36, 5-6, p. 422.

<sup>18</sup> Krylova, Y. (2018) *Corruption and the Russian Economy: How Administrative Corruption Undermines Entrepreneurship and Economic Opportunities*, London; New York: Routledge, p. 84.

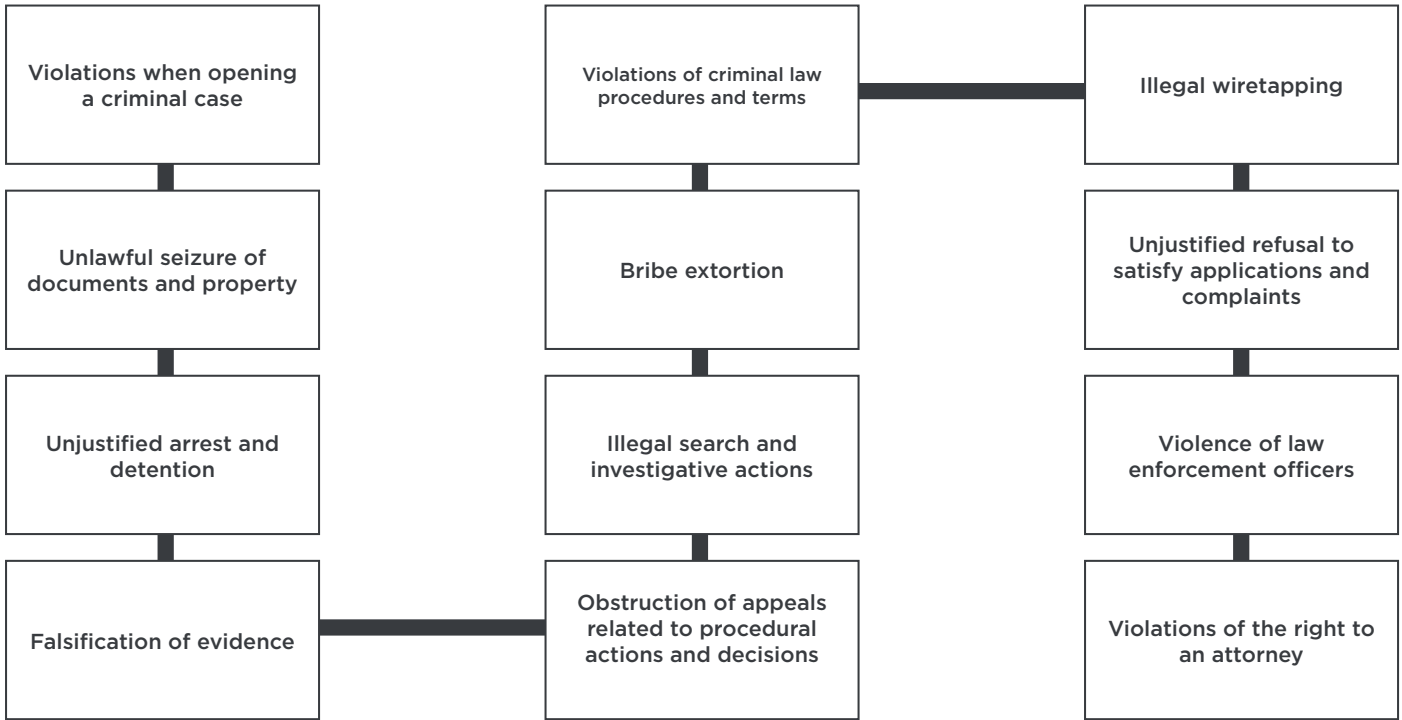
<sup>19</sup> Ruvinsky, V. (2019) "Zhaloby naverkh i v nikuda" [in Russian], *Vedomosti*, May 29, <https://www.vedomosti.ru/opinion/articles/2019/05/29/802688-zhalobi-naverh>, accessed February 10, 2021.

official complaints represent only a small fraction of the violations of entrepreneurial rights, they provide evidence of widespread corruption in Russia’s law enforcement. The portal “ZaBiznes” registered a wide range of law enforcement

violations, from opening bogus criminal cases against legal business owners to obstruction of their appeals related to procedural actions and decisions. Our analysis shows that almost any business can become a victim of unjustified

criminal prosecution and harassment by law enforcement, ranging from a home-based childcare business to a large profitable investment fund. Larger cases are often linked to technical-capacity and large-scale infrastructure projects.

**FIGURE 4 : VIOLATIONS OF THE RIGHTS OF ENTREPRENEURS BY LAW ENFORCEMENT**



**SNAPSHOT 1: RAIDING A KINDERGARTEN - THE CASE OF VASILY LIMONOV**

In 2013, Vasily Limonov organized a private kindergarten *Kuvshinka* in his home to provide daycare services for children. The district administration, which provided subsidies for his business, received all proper documentation, with full information about his business activities. Under federal law, such childcare facilities are not considered educational organizations, meaning that they do not require a license. Nevertheless, in 2016, officers from the Economic Security Unit, following an anonymous complaint, raided the kindergarten premises, seizing all business documentation and a computer. In addition, a criminal case was opened against the entrepreneur under Article 171 of the Criminal Code (carrying out entrepreneurial activity without a license). According to investigators, the damage was estimated at 2 million rubles (about \$33,000 in 2016). The criminal prosecution of the entrepreneur lasted more than a year. Only after the Russian business ombudsman’s intervention and clarifications from the Ministry of Education and Science, was the criminal case against Limonov finally terminated for lack of corpus delicti.

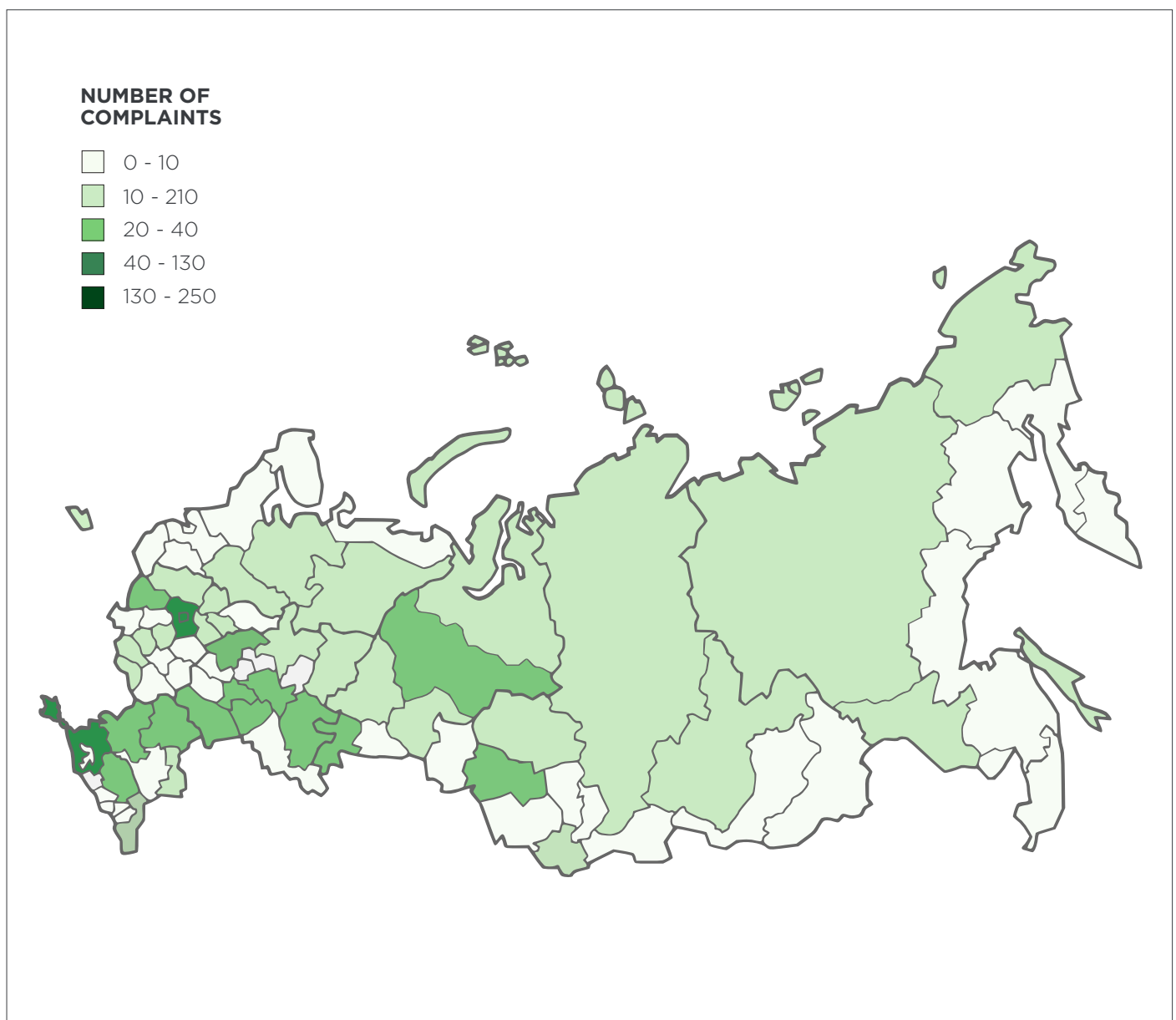
<sup>20</sup> Center for Public Procedures “Business Against Corruption” (2017) “Ugolovnoye delo v otnoshenii rukovoditelya detskogo sada «Kuvshinka» prekrashcheno” [in Russian], <http://www.nocorruption.biz>, accessed February 1, 2021.

**Geographically, complaints about violations of entrepreneurial rights come from various Russian regions.** The City of Moscow, with the highest number of complaints, represents an epicenter of the illegal raiding pandemic, followed by the Krasnodar region with the largest resort city of Sochi,

the Moscow region, and the City of St. Petersburg.<sup>21</sup> Together, these regions are responsible for over one third of the total entrepreneurial complaints received by the portal “ZaBiznes” in 2020. The geographical distribution of illegal raiding is mostly determined by industrial development and protection

of property rights at the regional level. Large cities that are home to significant numbers of businesses and entrepreneurial projects tend to rank higher on reiderstvo. In addition, regulatory and entrepreneurial policies, as well as levels of corruption, differ significantly in various regions within Russia.<sup>22</sup>

**FIGURE 5 : REGIONAL GEOGRAPHY OF ENTREPRENEURIAL COMPLAINTS RECEIVED BY THE PORTAL “ZABIZNES”**



<sup>21</sup> ANO Platform (2021) Statistics, <https://забизнес.рф/issues>, accessed February 1, 2021.

<sup>22</sup> Krylova, Y. (2018) “Administrative Corruption and its Effects on Russian Entrepreneurs: A Regional Aspect,” *Journal of Small Business & Entrepreneurship*, 3(3), 121–37.

Although the official website of Russia’s ombudsman posts some success stories where they helped entrepreneurs to close bogus criminal cases and restore their rights, the results of the 2019 Federal Guard Service survey shows that the vast majority of those attacked partially or entirely lost their assets. Particularly in those cases

where raiding attacks are initiated by security officers, it is extremely difficult for entrepreneurs to fight back, because the former have the entire state apparatus on their side. The story of a Magadan entrepreneur, Valery Khozhilo, illustrates the impediments that one might face in the fight against “raiders in uniform.”

Altogether, Khozhilo filed over 60 official complaints about the illegal seizure of his businesses and property theft, but all of them were rejected by the authorities, probably because the raid against him was organized by a Federal Security Service (FSB) officer.<sup>23</sup>

## SNAPSHOT 2: RAIDERS IN UNIFORM - THE CASE OF VALERY KHOZHILLO

In 2019, a well-known businessman in the Magadan region, Valery Khozhilo, filed a complaint to Russia’s business ombudsman about a criminal case allegedly fabricated against him by a FSB officer in the Samara region in order to seize his auto transport enterprises *Avtotek*, *Departament*, and *Magadan Avtosouz*. Khozhilo recalls that he became aware of the raiding attack in April of 2019, when he received an audio recording of a conversation between the FSB officer and another raider, where the FSB officer allegedly confessed to stealing accounting and legal documents from his companies. Immediately, Khozhilo wrote a complaint to the military prosecutor’s office. After that, events developed very rapidly. Khozhilo was charged with tax evasion and participation in a criminal conspiracy to receive unlawful tax deductions, and the police issued an arrest warrant for him. According to Khozhilo, the FSB officer used two of his personal friends as prosecution witnesses in the criminal case and also abducted and pressured another witness to give false testimony. The proof was the audio recording that the witness made on the phone during her abduction, as well as her own statement to the prosecutor’s office. According to Khozhilo, the FSB officer could exert force and moral pressure on other witnesses too. Meanwhile, the general director in the raided company was replaced, as evidenced by the falsification of the minutes of the general meeting, as well as the falsification of a number of notarial documents.<sup>24</sup>

## WHAT CRIMES ARE COMMITTED BY ILLEGAL RAIDERS?

There is no legal definition of “reiderstvo” in the Russian Criminal Code, although there have been proposals to add a special article to the

Code prescribing criminal sanctions for this type of crime. However, at each stage of the raiding process, raiders employ tactics and carry

out illegal activities that are addressed in a number of Russia’s Criminal Code articles.

<sup>23</sup> Rossiyskiy biznesmen pozhalovalsya na reyderskiy zakhvat yego kompaniy sotrudnikom FSB” [in Russian] (2020) *Rambler News*, July 20, <https://news.rambler.ru/other/44535297-rossiyskiy-biznesmen-pozhalovalsya-na-reyderskiy-zahvat-ego-kompaniy-sotrudnikom-fsb/>, accessed February 1, 2021.

<sup>24</sup> “Magadanskiy biznesmen obvinil sotrudnika FSB v reyderstve” [in Russian] (2020) *RosInform News Agency*, July 20, <https://rosinform.press/magadanskiy-biznesmen-obvinil-sotrudnika-fsb-v-rejderstve/>, accessed February 1, 2021.

**FIGURE 6 : RUSSIAN RAIDING CASES AND THE EMPLOYED TACTICS**

| Company (year when raids started) | Forgery and fraud | Malicious Prosecution | Tax Inspections | Misuse of Shares | Misuse of the Banking System | Violence | Dark PR | Abuse of the Rule of Law |
|-----------------------------------|-------------------|-----------------------|-----------------|------------------|------------------------------|----------|---------|--------------------------|
| Hermitage Capital (2005)          | ●                 | ●                     | ●               |                  |                              | ●        | ●       | ●                        |
| ToAZ (2004)                       | ●                 | ●                     | ●               | ●                | ●                            | ●        | ●       | ●                        |
| Yevroset (2002)                   | ●                 | ●                     | ●               |                  |                              | ●        |         | ●                        |
| Yukos (2003)                      | ●                 | ●                     |                 | ●                | ●                            | ●        | ●       | ●                        |
| KZM (2016)                        | ●                 | ●                     |                 | ●                | ●                            |          |         | ●                        |
| Rodina (2012)                     | ●                 | ●                     | ●               | ●                | ●                            |          |         | ●                        |
| Vkontakte (2011)                  |                   | ●                     |                 | ●                |                              | ●        | ●       | ●                        |
| Avtotek (2019)                    | ●                 | ●                     | ●               | ●                |                              | ●        | ●       | ●                        |
| Baring Vostok (2019)              |                   | ●                     |                 |                  | ●                            | ●        | ●       | ●                        |
| EnergoTrest (2014)                | ●                 | ●                     |                 |                  |                              |          |         | ●                        |
| Nginx (2019)                      |                   | ●                     |                 |                  |                              |          |         | ●                        |

The preparation stage of a raid often involves an illegal receipt and disclosure of information classified as commercial, tax, or banking secrets (Article 183 of the Criminal Code) from public officials, who can be bribed by private raiders or who can use this information themselves to organize raids against businesses. The second stage often involves such crimes as extortion, compulsion to complete a deal, obstruction of lawful

business activities, and abuse of authority (Articles 183, 179, 169, and 210 of the Criminal Code). If legal owners refuse to negotiate, the third stage is the execution of takeovers. Among many options available to raiders are fraud, registration of illegal deals, lawless actions in the case of bankruptcy, abuse of authority by private notaries and auditors, official forgery, fabrication of criminal cases, and theft or damage of

documents, stamps, or seals (Articles 159, 170, 195, 196, 197, 202, 292, 299, 305, and 325 of the Criminal Code). This stage requires the direct or indirect involvement of a large number of public officials. Once a takeover is completed, raiders can begin the process of laundering illegally acquired funds and property (Articles 174 and 175 of the Criminal Code).

**FIGURE 7 : ARTICLES OF THE RUSSIAN CRIMINAL CODE RELATED TO THE FOUR-STAGE RAIDING PROCESS**

|                     |  |
|---------------------|--|
| <b>Preparation</b>  | Art. 183 Illegal receipt and disclosure of information classified as commercial, tax, or banking secrets, Art. 272 Illegal accessing of computer information, Art. 290. Bribe-taking, Art. 291 Bribe-giving  |
| <b>Negotiation</b>  | Art. 183 Illegal receipt and disclosure of information classified as commercial, tax or banking secrets, Art. 272 Illegal accessing of computer information, Art. 290. Bribe-taking, Art. 291 Bribe-giving   |
| <b>Execution</b>    | Art. 159 Fraud, Art. 170 Registration of illegal land deals, Art. 185 Abuse related to securities issuance, Art. 195-197 Lawless actions in case of bankruptcy, deliberate and fictitious bankruptcy, Art. 202 Abuse of authority by private notaries and auditors, Art. 285 Abuse of official powers, Art. 292 Official forgery, Art. 299 Knowingly bringing an innocent person to criminal responsibility, Art. 301 Illegal detention, Art. 305 Knowingly giving an unjust judgement, decision, or any juridical act, Art. 325 Theft or damage of documents and seals, Art. 327 Forgery, manufacture, or sale of falsified documents, Art. 330 Arbitrariness |
| <b>Legalization</b> | Art. 174 The legalization (laundering) of funds and other property acquired in an illegal way, Art. 175 Acquisition or sale of property, knowingly obtained in a criminal manner, Art. 198-99 Tax evasion  |

**In the most complicated disputes, which can last for decades, raiders often use the so-called “cascading” technique to speed up a sequence of attacks on legal business owners through a combination of multiple methods.<sup>25</sup>** They include forgery and

fraud, malicious criminal prosecution, inspections by regulatory agencies, the misuse of the banking system, violence, black PR campaigns, and the abuse of the rule of law and international institutions. One of the most illustrative examples of the “cascading” technique

is the case of *TogliattiAzot* (ToAZ), the largest ammonia producer in Russia. Beginning in 2005, a series of minority shareholders, most recently represented by Dmitry Mazepin of *Uralchem*, have been pursuing different legal and extra-legal methods to take over the company.

<sup>25</sup>Beliakov, A. (2012) “Reiderstvo,” Echo of Moscow, March 7, <https://echo.msk.ru/blog/belyakov/866245-echo/>, accessed February 26, 2021.

### SNAPSHOT 3: THE “CASCADING” TECHNIQUE – THE CASE OF TOAZ

Since 2005, one of Russia’s largest ammonia producers *ToAZ* experienced several raiding campaigns based on a cascade of multiple methods, ranging from semi-legal to illegal, applied sequentially or simultaneously. In the *ToAZ* case, the cascade of tactics flowed upward on the scale of harassment, from an initial offer to buy the controlling stake to the abuse of the police and enforcement agencies; the misuse of tax inspections to bankrupt the company; fabricated civil and criminal cases on charges of fraud, tax evasion, and embezzlement; extradition requests and Red Notices issued on the *ToAZ* former President and CEO, Vladimir Makhlai, his son, Sergey Makhlai, who replaced him as CEO in 2011, and the leadership of Swiss agribusiness *Ameropa Holding*. The Red Notices were eventually thrown out and an extradition request against then *ToAZ* CEO Evgeny Korelev rejected. To discredit the Makhlais in the eyes of the business community, *ToAZ* employees, and the public, the raiders allegedly hired black PR professionals who prepared “a series of incriminating materials” and “a number of fictitious situations” to imprison *ToAZ*’s top managers.

In the first wave of attacks, it took the Makhlais almost five years to prove that their criminal prosecution on embezzlement and fraud charges was ungrounded. Yet, in 2012, during the second wave, the raiders initiated criminal investigations with exactly the same allegations. In 2019, the Komsomolsky District Court of Togliatti sentenced Vladimir Makhlai and Sergey Makhlai to nine years in prison in absentia for embezzlement. In 2020, the Samara Regional Court upheld this conviction. In response, Sergey Makhlai published an open letter addressed to Russia’s Prosecutor General, in which he denied any wrongdoing and expressed his concerns about the quality of prosecutorial supervision and law enforcement in Russia. Indeed, during this almost decade-long legal fight, there have been multiple documented accounts of fabricated evidence, questionable expert reports, bribed witnesses, anonymous testimonies, and so-called “telephone justice” in the form of informal influence and pressure on the judiciary. In the hope for justice, in 2016, *ToAZ*’s majority shareholders filed claims in Ireland against *Uralchem* and other actors, alleging of “vexatious litigation and raiding attempts to seize control of *ToAZ*.”<sup>26</sup>

**At the final stage, raiders often try to re-register property through shell companies to establish a good faith purchaser exemption and launder their raided property.** Even if legal owners can prove the fact of raiding, they are often unable to recover their assets and businesses. If courts

recognize a third party who acquired the stolen assets as a good faith purchaser, judicial practice limits recovery of the assets. Laundering of raided property is often based on the collusion of criminal groups with registration agencies. The most effective way to restore the rights of legal business owners would be through the

identification of beneficial owners of shell companies, however, this is not required in Russia. Another measure against such violations would be to increase the effectiveness of international financial institutions in reporting suspicious transactions.

<sup>26</sup> Foxall, A. (2020) *Russian ‘Black PR’: Examining the Practice of Ruining Reputations*, London: Henry Jackson Society; Coalson, R. (2008) “The Myth of Putin’s Popularity,” RFE/RL, December 30, <http://www.rferl.org/content/blog/1365202.html>, accessed March 16, 2016; Akimov, I. (2020) “Vazhno, chtoby rassledovaniye ‘dela ToAZ’ stalo po-nastoyashchemu ob’yektivnym” [in Russian], *Gazeta.Ru*, August 25, <https://www.gazeta.ru/social/2020/08/25/13210891.shtml>, accessed February 1, 2021; Williams, C. (2017) “Court Rejects Russian Extradition Bid,” *The Telegraph*, January 2, <https://www.telegraph.co.uk/business/2017/01/02/court-rejects-russian-extradition-bid/>, accessed March 24, 2021; Keena, C. (2016) “Russia ‘Raider Attack’ Case Makes it to the High Court,” *The Irish Times*, November 12, <https://www.irishtimes.com/business/energy-and-resources/russia-raider-attack-case-makes-it-to-the-high-court-1.2864787>, accessed March 24, 2021.



## WHY IS ENTREPRENEURSHIP CONSIDERED ONE OF THE MOST DANGEROUS OCCUPATIONS IN RUSSIA?

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There has been growing evidence that in many cases, not only do Russia's law enforcement agencies fail to criminally prosecute illegal raiders, but instead they also detain, arrest, intimidate, and imprison legal business owners in order to facilitate raiding attacks. The rise of raiding cases that involve malicious criminal prosecution of businessmen explains why entrepreneurship is considered one of the most dangerous occupations in

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"It is hard to find another social group persecuted on such a large scale [as Russian businessmen]."

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Russia. According to Russia's business ombudsman, "it is hard to find another social group persecuted on such a large scale [as Russian businessmen]."<sup>27</sup> Malicious criminal prosecution often involves economic crimes,

Articles 159, 160, and 165 of the Criminal Code are often called "rubber" articles, meaning that one can easily bend them in their own interests.

such as fraud (Article 159 of the Criminal Code), embezzlement (Article 160), and infliction of financial damage or losses by means of deceit or abuse of trust (Article 165).

**Current provisions of the Criminal Procedure Code cannot effectively protect businessmen who are unjustly charged with economic crimes.** Importantly, there are no clear criteria of classifying crimes in the entrepreneurial sphere. Chapters 21 and 22 of the Criminal Code provide a broad list of economic crimes that are subject to varying interpretations. Particularly, Articles 159, 160, and 165 of the Criminal Code are often called "rubber" articles,<sup>28</sup> meaning that one can easily bend them in their own interests. In some

cases, a simple failure to fulfill contractual obligations can be treated as fraud and lead to a criminal case. The lack of a uniform legal approach to the classification of economic crimes gives wide discretion to the police and judges in applying Chapters 21 and 22 of the Criminal Code to business activities.

One of the most recent examples of how the "rubber articles" of the Criminal Code can be misused to put pressure on prosperous businesses is the criminal case against Michael Calvey, an American businessman known as one of the most successful private foreign investors in Russia. The *Baring Vostok* fund, headed by Calvey, invested in many successful Russian projects, from *Yandex*, Russia's tech giant that competes with *Google*, to *Ozone*, one of the largest e-commerce platforms often called "the Amazon of Russia."

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<sup>27</sup> Cited in Kesby, R. (2012) "Why Russia Locks up so Many Entrepreneurs," *BBC News*, July 5, <http://www.bbc.com/news/magazine-18706597>, accessed February 8, 2021.  
<sup>28</sup> Titov: okolo 85% del protiv predprinimateley vzbuzhdayetsya po stat'ye 'moshennichestvo'" [in Russian] (2019) TASS, September 5, <https://tass.ru/ekonomika/6849457>, accessed February 26, 2021.

## SNAPSHOT 4: BUSINESS BEHIND BARS - THE CASE OF BARING VOSTOK

Michael Calvey, the founder of the *Baring Vostok* investment fund, was detained in Moscow in February 2019. He and his five colleagues were charged with fraud, which was later re-qualified to embezzlement in the amount of 2.5 billion rubles (about \$41 million in 2019) through the issuance of a bad loan. All defendants denied any wrongdoing. The criminal charges were allegedly related to a corporate dispute with businessman Artem Avetisyan's *Finvision Holdings* over the control of the Russian *Vostochny Bank*. Before he was transferred to house arrest in April 2019, Calvey spent several weeks in Moscow's notorious Matrosskaya Tishina Prison, where Sergei Magnitsky died in 2012. The same detective who prosecuted Magnitsky was assigned to his case.

Many representatives of the Russian business community spoke out in defense of Calvey. Even Putin's ally, Russia's ex-finance minister Alexei Kudrin, called Calvey's arrest an "economic emergency." Alexis Rodzianko, President of the American Chamber of Commerce in Russia, indicated that the charges against Calvey were without legal merit, while his arrest stemmed from "a commercial dispute in the usual sense." There was no victim in the case either: *Vostochny Bank* withdrew the civil case in October 2020, when the parties to the conflict, *Evison Holdings* controlled by *Baring Vostok* and Avetisyan's *Finvision Holdings*, announced the settlement of all claims against each other. In addition, Calvey repaid 2.5 billion rubles to *Vostochny Bank*. However, the criminal case against Calvey was not closed. In February 2021, the Moscow court began the criminal embezzlement trial of Calvey and his colleagues despite the settlement with *Finvision Holdings*. If convicted, they might face up to ten years of imprisonment.<sup>29</sup>

The arrest and imprisonment of Calvey shocked the Russian and international investment community and provoked an outcry in the media. However, long before *Baring Vostok*, there had been similar cases involving Russian entrepreneurs who received little or no attention in the media. In a recent case, for example, Artem Potekhin and Sergei Konchenkov, who headed *EnergoTrest LLC*, a power company in the Tver region, were charged with fraud. They spent about four years in a pre-trial detention

center despite the fact that the arbitration court issued a decision in their favor and against their competitor who allegedly accused them of fraud in order to seize their assets.<sup>30</sup>

**Charges in tax violations, including tax evasion under Article 199 of the Criminal Code, represent another popular raiding tactics for several reasons.** First, *tax violations in Russia are over-criminalized*, meaning that even those actions that are the result of minor errors

in economic activities of enterprises and that do not entail any serious damage can be qualified as crimes. Second, *the related charges might be very arbitrary due to weak coordination between investigative and tax authorities*, as well as the lack of specific provisions defining tax fraud and value-added tax (VAT) fraud in the national legislature. Third, *Russian tax legislation is very complex and changes very rapidly, with multiple amendments introduced every year.*

<sup>29</sup> "Russia Cancels House Arrest of U.S. Investor Calvey, Other Suspects In Embezzlement Case" (2020) RFE/RL, November 12, <https://www.rferl.org/a/russia-cancels-house-arrest-of-u-s-investor-calvey-other-suspects-in-embezzlement-case/30944836.htm>, accessed February 3, 2021; Cobus, P. (2019, February 21) "American's Detention Potentially Decisive Moment for Russia, Trade Groups Say," *VOA*, <https://www.voanews.com/europe/americans-indictment-potentially-decisive-moment-russia-trade-groups-say>, accessed February 3, 2021.

<sup>30</sup> Center for Public Procedures "Business Against Corruption (2018) "Tverskiye energetiki – figuranty rossiyskogo «spiska Titova» – vpushcheny pod zalog nezadolgo do vyneseniya prigovora" [In Russian], <http://www.nocorruption.biz>, accessed February 12, 2021.

**Malicious prosecution of Russian entrepreneurs is not limited to fabricated charges of economic crimes or tax evasion.** There is a formidable arsenal of other charges that can be filed against businessmen targeted by raiders and opponents, starting from intellectual property violations to outright murders. For example, in the infamous Yukos case, Russia

issued a Red Notice on Mikhail Khodorkovsky on murder charges. This happened in 2015 and was allegedly related to a pro-democracy movement that Khodorkovsky founded in exile, following his release from prison after a presidential pardon in 2013.<sup>31</sup> Furthermore, malicious criminal prosecution of legal business owners is often combined with the misuse

of the banking system. An illustrative example is the case of Airat Amirov, an entrepreneur from the Tatarstan region, who in 2002 founded a profitable metalware plant, the *Kazanskiy Zavod Metalloizdeliy* (KZM), which was bankrupted by raiders and liquidated in 2019.

### SNAPSHOT 5: PET BANKS - THE CASE OF KZM

In 2020, Airat Amirov, the founder and former CEO of KZM, a large metalware plant, filed a complaint through the electronic portal “ZaBiznes” where he accused his former partner and a high-ranking official from the Regional Administration of orchestrating an illegal seizure of his plant, using *Sberbank*, the largest state-owned Russian bank, as a tool for “squeezing out” the business. In 2012, KZM received a five-year loan of 68 million rubles (about \$2.3 million in 2012). However, long before the deadline, *Sberbank* unexpectedly put forward an ultimatum to the businessman to pay off the entire balance. Due to unfavorable economic situation in Russia at that time, Amirov could not find enough financial resources and all his attempts to negotiate a debt restructuring were blocked at the regional level. Under the terms of the loan agreement, Amirov had the right to sell the machinery he bought with the loan to repay his debt in the pretrial order. According to Amirov, the buyer offered twice the balance on the loan, but *Sberbank* refused to agree to the sale. This refusal, according to Amirov, came from the Regional Administration. After *Sberbank* filed the bankruptcy claim, it immediately resold the plant’s debt for a much lower amount to a company affiliated with the raiders. Not only did Amirov’s attempts to bring the raiders to justice not generate any results, but instead Amirov himself became a victim of criminal prosecution. In April 2019, a criminal case was opened under Article 196 of the Criminal Code (deliberate bankruptcy), which Amirov links to his raiders’ use of security officials to cover up their illegal actions.<sup>32</sup>

**This hostile business environment has been damaging to Russia’s economy, as many Russian entrepreneurs live in self-imposed exile and are building up their businesses outside Russia.** In recognition of this issue, Boris Titov, Russia’s business ombudsman, has pushed for an amnesty for entrepreneurs who

were unjustly charged with economic crimes in Russia, and in 2018, developed the “Titov List” of businessmen who wanted to come back to Russia in return for an amnesty. Russian authorities agreed to give them a chance to defend themselves in court if they returned home. However, this option seemed less than desirable after the

first businessman from the Titov list to return to Russia, Andrei Kakovkin, was arrested upon his arrival. Although later the police released him and closed the criminal case, it was resumed one month later, and Kakovkin was sentenced to three years in prison, which was subsequently replaced by a suspended sentence.<sup>33</sup>

<sup>31</sup> “Murder Charges Against Khodorkovsky” (2015) *RFE/RL*, December 11, <https://www.rferl.org/a/khodorkovsky/27420886.html>, accessed February 16, 2021.

<sup>32</sup> “Kreditnoye reyderstvo: ruchnoy Sberbank na podkhvate u ministra” [in Russian] (2020) *PASMI.ru*, February 21, <https://pasmir.ru/archive/259646/>, accessed February 15, 2021.

Yevgeny Chichvarkin was probably one of the most skeptical entrepreneurs about the Titov list. Chichvarkin has been residing in London ever since *siloviki* raided his company *Yevroset*, Russia's largest mobile phone retailer, charging him with extortion and kidnapping. Although all charges against him were

dropped in 2011, when he sold his company, he continues to refuse to return to Russia under the current political regime. As he predicted one month before the 2018 Presidential elections, "[b]usiness in Russia will keep being raided and pressured with special cynicism after the elections. Putin doesn't

need private business...We are waiting for a new influx of emigration." Another prominent example of the Russian entrepreneurs who live in self-imposed exile is Pavel Durov, the founder of *VKontakte* (VK), Russia's most successful social network, similar to Facebook.

## SNAPSHOT 6: RUSSIA'S ZUCKERBERG IN EXILE - THE CASE OF PAVEL DUROV

Pavel Durov's problems with Russia's authorities started in 2011, when he refused to shut down pages of opposition politicians in the *VK* social network he founded in 2006. These problems were exacerbated in 2014 when Durov refused to hand over data of Ukrainian Euromaidan protesters to Russia's security officers and block opposition leader Alexei Navalny's page. The campaign organized against Durov included police searches in his apartment and the *VK* headquarters, a smear campaign, and a hostile takeover of his social network by a Kremlin-friendly businessman who was allegedly connected to the *Yukos* case. According to the police, Durov was investigated regarding an incident where a traffic policeman was allegedly injured by an unidentified driver. Durov's spokesman, however, stated that the founder of *VK* did not even own a car. As the result of state pressure, Durov was dismissed as CEO of *VK* and was forced to leave the country. Yet, the battle was not over.

Upon leaving Russia, Durov focused on developing *Telegram*, a freeware, cloud-based instant messaging app, which became very popular in Russia and other countries. In 2018, Russia's authorities requested access to users' encrypted messages on *Telegram*. When Durov refused them once again, Russia's state telecommunications regulator, Roskomnadzor, banned the app in the country. In response, *Telegram* launched the digital resistance initiative, with a network of anonymous developers creating proxy servers that successfully made the app accessible to all Russian users despite the ban. Two years later, recognizing its failure, Roskomnadzor lifted its own ban. Eventually, Durov secured his victory over Russia's authorities: *Telegram*'s users exceeded 400 million people worldwide, including 30 million users in Russia.<sup>35</sup>

<sup>33</sup> "Court Replaces Prison Term with Suspended Sentence for Rostov Businessman from 'Titov List' Convicted of Fraud" (2021) *Interfax*, January 22, <https://interfax.com/news-room/top-stories/17817/>, accessed February 3, 2021.

<sup>34</sup> Chichvarkin, Y. (2018) "Vchera priyetzhal Boris Titov" [in Russian], Facebook, February 4, <https://www.facebook.com/photo.php?fbid=1953946418189850&set=a.1745825792335248.1073741831.100007235320406&type=3&theater>, accessed February 3, 2021.

<sup>35</sup> Bidder, B. (2013) "Kremlin Targets Russian Facebook Clone VKontakte," *Der Spiegel*, May 2; Khurshudyan, I. (2020) "How the Founder of the Telegram Messaging App Stood up to the Kremlin — and Won," *Washington Post*, June 28.

## HOW DO RAIDERS MISUSE INTERNATIONAL INSTITUTIONS?

### Due to systemic corruption, it is relatively easy for raiders to obtain a desired ruling in Russian court proceedings.

This is why in many cases, Western courts represent a last resort for legal owners of Russian businesses to fight back against their raiders. An illustrative example is the longstanding dispute between the management

of *TogliattiAzot* and its minority shareholder *Uralchem*.<sup>36</sup> In 2016, *ToAZ's* shareholders filed a claim in the High Court in Ireland against Dmitry Mazepin, *Uralchem*, and *Eurotoaz*, a company involved in the raiding campaign. In 2019, following the Irish High Court order, *Uralchem* undertook a written commitment not to

enforce any damages claim in the Russian proceedings against the plaintiffs or their assets until the end of the proceedings in Ireland,<sup>37</sup> which are still going on as of February 2021. In such cases, it is important that Western legal experts learn how to identify the “red flags” of criminal raiding.

### SNAPSHOT 7: RED FLAGS FOR CRIMINAL RAIDING

Increasingly, the courts and arbitration bodies of Western countries are being faced with complex corporate cases from Russia. In many of them, the mass of documentation provided is opaque and makes it difficult to distinguish a legitimate business dispute from a criminal raid. Every raiding case is different, but there are often common features that can provide red flags to practitioners in this field. These include:

- The original owners of the asset in question were charged and/or detained under Articles 159, 160 or 165 of the Russian Criminal Code.
- Black PR on the owner and the business appear before and during the raid.
- Loans to the business are called in before their term, without any adequate explanation or notice, especially by state-associated banks.
- Individuals associated with other raids are added to the company's board or management team.
- Network analysis reveals that consulting firms “hired” to evaluate and restructure the business are associated with the raiders.
- Raiders employ facilitators associated with other raids, such as notaries who have previously post- or pre-dated key documents.
- Raiders use orchestrated bankruptcies to take over the business.
- The new owners make no effort to help the company in crisis, instead introducing “professionals” to the management team who may intentionally undermine the business.
- The raider uses accountants who produce accounts often based on inaccurate information provided by the raider.
- Network analysis demonstrates linkages between the new owners and a new or more powerful clan of corrupt oligarchs.

<sup>36</sup> Carolan, M. (2019). “High Court Rules in Case of Four Caribbean-Registered Firms,” *The Irish Times*, January 18, <https://www.irishtimes.com/business/manufacturing/high-court-rules-in-case-of-four-caribbean-registered-firms-1.3763154>, accessed February 10, 2021.

<sup>37</sup> ToAZ (2020) “The High Court of Ireland Confirmed Its Decisions in Regards with the Foreclosure of PJSC TOAZ Shares,” <https://www.toaz.ru/en/media-centre/news/2020/the-high-court-of-ireland-confirmed-its-decisions-in-regards-with-the>, accessed February 26, 2021.

At the same time, Russian raiders often misuse legal procedures in Western courts and arbitration bodies requesting legal actions against victims of raiding attacks based on rulings of Russian courts. In such cases, it is up to Western judges to decide whether foreign judgements were valid, however, their ability to make such assessments might be limited by available information. *The ability of raiders and corrupt officials to exploit legal proceedings in Western countries depends on whether judges are aware of corruption in Russia and other authoritarian countries.* Yet, even a widely-shared consensus about corruption in these countries cannot guarantee that raiders or corrupt officials will be held legally accountable for their actions. This is evident from a recent case where a Swedish court of appeal upheld the acquittals of former senior officials whose telecom company admitted to bribing the daughter of Uzbekistan's former president, Gulnara Karimova, to get licenses to do business in that country.<sup>38</sup> The Swedish court ruled in favor of the defendants, based on the claim that "it had not been proven that Karimova

held any official position connected to the telecom sector."<sup>39</sup> This happened despite the fact that the former president's daughter, an infamous kleptocrat, had been found guilty in 2020 of extortion, money laundering, misappropriating the property of others, and financial and other crimes by Uzbekistan's Supreme Court and sentenced to 13 years of imprisonment.

**The proportion of litigants from Russia and other former Soviet republics significantly increased in foreign courts in the last years.** According to the 2020 report by Portland, a strategic communications consultancy based in the United Kingdom, for the fifth year in a row, Russia's litigants continued their prominence, particularly in major civil fraud and investigations cases.<sup>40</sup> The number of similar cases in the U.S. courts have also been on the rise. Manipulative and exploitative practices used by Russian state actors and raiders in U.S. courts have been recently well documented, including the abuse of Section 1782 of Title 28 of the United States Code on judiciary and judicial procedure, Chapter 15 of the U.S. Bankruptcy Code, and actions for recognition

or enforcement of Russian judgments.<sup>41</sup>

**Russian raiders take advantage of the process of discovery and mutual legal assistance treaties to collect financial information on their political and economic opponents in various countries.**

In May 2020, for instance, the Swiss federal prosecutor office drew complaints when it intended to share sensitive information, including the testimony and witness statements related to the Magnitsky case and the Russian tax fraud with the Kremlin.<sup>42</sup> Yet, not all efforts to misuse legal procedures in Western courts and arbitration bodies are successful. For example, in the infamous raiding case against *TogliattiAzot*, a recent attempt to abuse a disclosure procedure in the U.S. courts failed when a U.S. Magistrate Judge denied the disclosure on the grounds that the "requested evidence was not necessary for the Russian proceedings."<sup>43</sup> In another case of aggressive insolvencies against Natalia Pirogova, the U.S. courts denied recognition of the Russian bankruptcy due to lack of sustained ties between the debtor and Russia.

<sup>38</sup> "Stockholm Court Upholds Telia Acquittals in Gulnara Karimova Case" (2021) *RFE/RL*, February 5, <https://www.rferl.org/a/uzbelkistan-stockholm-court-upholds-telia-acquittals-gulnara-karimova-case/31087633.html>, accessed February 10, 2021.

<sup>39</sup> Miller, H. (2020) "Daughter of Late Uzbek President Gets Shot at Frozen Fortune," *Al Jazeera*, December 3, <https://www.aljazeera.com/economy/2020/12/3/bbdaughter-of-late-uzbek-president-gets-shot-at-frozen-fortune>, accessed February 10, 2021.

<sup>40</sup> Portland (2021) *2020 Commercial Courts Report*, [https://portland-communications.com/wp-content/uploads/2020/05/Commercial-Courts-Report-2020.pdf?utm\\_medium=email&utm\\_campaign=Send%20Report&utm\\_content=Send%20Report+&utm\\_source=Email%20marketing%20software&utm\\_term=here](https://portland-communications.com/wp-content/uploads/2020/05/Commercial-Courts-Report-2020.pdf?utm_medium=email&utm_campaign=Send%20Report&utm_content=Send%20Report+&utm_source=Email%20marketing%20software&utm_term=here), accessed February 10, 2021.

<sup>41</sup> Åslund, A. (2018) *Russia's Interference in the US Judiciary*, Washington, D.C.: Atlantic Council.

<sup>42</sup> Jones, S. (2020) "Browder Vows to Fight Swiss Legal Co-Operation with Russia," *Financial Times*, May 13, [https://www.swissinfo.ch/eng/michael-lauber\\_browder-vows-to-fight-swiss-legal-co-operation-with-russia-/45756350](https://www.swissinfo.ch/eng/michael-lauber_browder-vows-to-fight-swiss-legal-co-operation-with-russia-/45756350), accessed February 10, 2021.

## SNAPSHOT 8: DEFENCE AGAINST AGGRESSIVE RUSSIAN INSOLVENCIES - THE CASE OF NATALIA PIROGOVA

A Russian businesswoman, Natalia Pirogova, became subject of a Russian insolvency proceeding in 2015 after she failed to repay an alleged \$18.5 million bank debt. In Russia, she faced civil and criminal actions for a loan that her company, *Rizalti-Plus-DKD*, obtained in 2007. Another of her companies, *Taurus LLC*, was liquidated in 2017 Russian bankruptcy proceedings. In 2018, Yuri Rozhkov, a trustee in the Russian proceedings, filed a petition in the Southern District of New York Bankruptcy Court to recognize the Russian Insolvency Proceeding under Chapter 15 of the U.S. Bankruptcy Code. According to Pirogova's defense, she was a victim of aggressive insolvency proceedings used by raiders to seize her assets in Russia, and she had to flee the country due to malicious criminal prosecution. The key defense strategy was to demonstrate lack of sustained ties between Pirogova and Russia, using her green card obtained in 2008, her marriage to an American citizen, and assets and creditors within the United States. Based on demonstrated evidence, the U.S. court ordered denying recognition of the Russian bankruptcy.<sup>44</sup>

**The issuance of Red Notices is another popular technique used by Russia to manipulate law enforcement in other countries into acting in the interests of raiders to detain, arrest, and extradite their victims, as well as to freeze their assets.** There is strong evidence that such misuse of Interpol undermines the asylum and judicial process in

the United States and other Western countries.<sup>45</sup> In 2018, a former Russian businessman who criticized corruption in Russia, Grigory Duralev, was arrested in Los Angeles by ICE on a Red Notice issued by Russian authorities. He faced deportation despite the fact that he was legally staying in the United States, awaiting a decision on his

asylum application.<sup>46</sup> Although the Red Notice on him was incomplete and inaccurate, Duralev was detained in a maximum-security facility for nearly 18 months.<sup>47</sup> Similarly, the case of the brothers Vladimir and Alexandr Kholodnyaks shows how the U.S. immigration process can be delayed by Red Notices issued by authoritarian states.

<sup>43</sup> "Uralchem Seeks Information Disclosure in U.S. courts amid Togliattiazot Case" (2020, August 18) RAPS, [http://www.rapsnews.com/judicial\\_news/20200818/306161223.html](http://www.rapsnews.com/judicial_news/20200818/306161223.html), accessed February 10, 2021.

<sup>44</sup> Kobre & Kim (2020) "New Tools to Defend against Aggressive Non-U.S. Insolvencies," *Disputes and Investigations*, <https://kobrekim.com/insights/client-alert/-new-tools-defend-against-aggressive-non-us-insolvencies>, accessed February 17, 2021; In Re: Natalia Mikhailovna Pirogova, No. 1:2019cv00231 (S.D.N.Y. 2020), <https://law.justia.com/cases/federal/district-courts/new-york/nysdce/1:2019cv00231/508081/16/>, accessed February 17, 2021.

<sup>45</sup> TraCCC (2018) *Spotlight on a Critical Threat: The Abuse and Exploitation of Red Notices, Interpol and the U.S. Judicial Process by Russia and Other Authoritarian States*, <https://traccc.gmu.edu/sites/default/files/TraCCC/Final-Red-Notices-Conference-Report-Bright-Red.pdf>, accessed February 10, 2021.

<sup>46</sup> Bertr, N. (2020) "He Fought Corruption in Russia. ICE Wants to Deport Him," *POLITICO*, September 3, <https://www.politico.com/news/2020/09/03/gregory-duralev-ice-deportation-408607>, accessed February 10, 2021.

<sup>47</sup> Ibid.

## SNAPSHOT 9: RAIDING “MOTHERLAND” - THE CASE OF RODINA

The case of the brothers Vladimir and Alexandr Kholodnyaks is a classic example of the illegal raiding playbook. Their construction company, *Rodina* (meaning “Motherland” in Russian), was allegedly raided by a competitor who held a position within the Regional Administration in the Krasnodar region. The longstanding raiding campaign involved the abuse of regulatory agencies, obstruction of business activities, violence, destruction of the company’s registration and financial documentation, and launching court proceedings against the owners, which resulted in a loss of over 200 million rubles (about \$3.56 million at that time). When civil and administrative actions did not generate any result, a criminal case was opened against the brothers on charges of fraud. Eventually, in 2014, the Kholodnyaks had to flee the country to the United States and apply for asylum. Yet, the Red Notices that the Russian state issued on them posed a serious problem for their immigration cases, as well as their professional, financial, and personal lives in the United States. In 2015, the brothers filed challenges to the Red Notices, however, it took them more than a year to remove their personal data from the Interpol system.<sup>48</sup>

### **Laundering of assets acquired through illegal raiding and corruption presents a critical challenge in today’s globalized world.**

The ill-gotten gains of Russian raiders are a sizeable component of the huge cash flows that are laundered through the financial system and real estate, primarily in Western countries. This inflow of dirty money, in turn, corrodes the financial and political institutions of

the recipient economies. A few examples of this trend are evident from the notorious Hermitage Capital Management case. In 2020, Latvia’s Economic Crime Bureau seized assets in the amount of \$0.5 million related to several Magnitsky cases.<sup>49</sup> In 2017, the Cypriot company, *Prevezon Holdings*, which was a beneficiary of Russia’s tax fraud related to the death of Magnitsky, paid about \$6 million to get

out from under U.S. money laundering charges. One of its attorneys was later accused of obstruction of justice and working for Russia to influence the 2016 U.S. presidential election.<sup>50</sup> In this context, the 2021 decision of the Swiss prosecutor’s office to shut down a Russian money laundering probe and unfreeze the related accounts in Credit Suisse and UBS caused an international outcry.<sup>51</sup>

<sup>48</sup> Estlund, M. (2017) “INTERPOL Red Notice Removal Cases - A Sample of Results from 2016, Part 1,” *The Red Notice Law Journal*, January 10, <https://www.rednoticelawjournal.com/2017/01/interpol-red-notice-removal-cases-a-sample-of-results-from-2016-part-1/>, accessed February 10, 2021; Kazakov, E. (2015, November 26) “Brat'yev Aleksandra i Vladimira Kholodnyakov Krasnodarskiy sud priznal bankrotami” [in Russian], *Komsomol'skaya Pravda*, <https://www.kp.ru/online/news/2233794/>, accessed February 10, 2021.

<sup>49</sup> “Latvian Police Seize Half a Million Dollars of ‘Magnitsky money’” (2020) LSM.lv (March 9, <https://eng.lsm.lv/article/society/crime/latvian-police-seize-half-a-million-dollars-of-magnitsky-money.a351052/>), accessed February 10, 2021.

<sup>50</sup> Radu P., Velikovskiy D., and Shmagun O. (2020) “Prevezon Holdings: The Black Money Collector,” *OCCRP*, November 17, <https://www.occrp.org/en/the-fincen-files/prevezon-holdings-the-black-money-collector>, accessed February 10, 2021.

<sup>51</sup> “A Swiss Money-Laundering Probe Raises Disturbing Questions” (2021) *Economist*, January 23, <https://www.economist.com/finance-and-economics/2021/01/23/a-swiss-money-laundering-probe-raises-disturbing-questions>, accessed February 10, 2021. This article raises concerns about corrupt relations between Swiss law enforcers and Russian counterparts.



**Money laundering in Western countries has many negative consequences for local communities and economies.**

The flood of Russian money has contributed to a bubble in asset and property prices in many cities, the dislocation of residents from and within major metropolitan areas, the threat of monetary instability due to the misallocation of

resources, the loss of policy control over the real estate and building industries, accumulation of political influence by foreign politically exposed persons, and the formation of hubs for other criminal activities. Money laundering also poses a national security threat by worsening instability in conflict and post-conflict

countries that are particularly vulnerable to corruption, violence, organized crime, and terrorist finance. Another threat to national security relates to the export of economic criminality from kleptocratic states to democratic countries through their financial and real estate channels.<sup>52</sup>

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## WHAT DOES THIS MEAN FOR BUSINESS AND RUSSIA'S ECONOMY?

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**Many economic opportunities are being irrevocably lost each year in Russia because of illegal business raiding, systemic corruption, and violations of entrepreneurial rights by law enforcement.**

The combination of these problems, together with recent economic recession, created a considerable drag on entrepreneurial activity. When asked about Russia's future economic development, Vladimir Perevezin, a Russian

entrepreneur who was a victim of criminal prosecution, said that "the economy will be completely destroyed because businessmen are not safe in the country – anyone could be sent to jail."<sup>53</sup>

**The decline of an entrepreneurial spirit is compounded by threats of unjust imprisonment.**

Even the most prominent foreign investors in Russia, such as Michael Calvey, are no exception. Calvey's arrest in 2019 showed to the world that in Russia, a manufactured criminal charge and threat of imprisonment can result from any business dispute. The case inflicted enormous damage to the Russian investment climate.

In the words of Bill Browder, "The arrest of Mike Calvey in Moscow should be the final straw that Russia is an entirely corrupt and uninvestable country."<sup>54</sup> In Calvey's own words, "I was charged with a serious crime and put on trial for a crime thought up by the investigators. Under these circumstances, the charge against me is not only unreasonable and unfair, but also illegal."<sup>55</sup> Such cases demoralize businesses. After all, the question is how much entrepreneurs are willing to invest in the country where their assets might be stolen and where they might find themselves behind bars just for developing a successful business.

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"The arrest of Mike Calvey in Moscow should be the final straw that Russia is an entirely corrupt and uninvestable country."

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<sup>52</sup> TraCCC (2017) *Money Laundering in Real Estate*, [https://traccg.gmu.edu/sites/default/files/2018-MLRE-Report\\_0.pdf](https://traccg.gmu.edu/sites/default/files/2018-MLRE-Report_0.pdf), accessed February 10, 2021.

<sup>53</sup> Cited in Kesby, R. (2012) "Why Russia Locks up so Many Entrepreneurs," *BBC News*, July 5, <http://www.bbc.com/news/magazine-1870659>, accessed February 10, 2021.

<sup>54</sup> Browder, B. [@Billbrowder] (2016) "The Arrest of Mike Calvey" [Tweet], *Twitter*, February 15, <https://twitter.com/billbrowder/status/1096393266407325697?lang=en>, accessed February 10, 2021.

<sup>55</sup> Rudnitsky, J.(2021). "Michael Calvey Trial: Russia Starts Embezzlement Case of Baring Vostok Capital – Bloomberg," *Bloomberg*, February 2, <https://www.bloomberg.com/news/articles/2021-02-02/russia-starts-embezzlement-trial-of-u-s-investor-calvey>, accessed February 10, 2021.

**These negative trends keep Russia's economy on an unproductive trajectory of a resource-dependent country that lacks modern technology and diversified production.** In 2020, net private capital outflow from Russia was estimated at \$47.8 billion, over twice the 2019 estimate.<sup>56</sup> Capital

flight is also accompanied by a brain drain as more and more talented entrepreneurs and educated young people leave the country. Some of the most prominent Russian tech entrepreneurs, such as the *Telegram* creator Pavel Durov, have chosen to live in self-imposed exile after they faced intimidation

and harassment by law enforcement in their own country. Many of the big names in IT in the United States and other countries are of Russian origin. A recent example is *Nginx*, one of the most successful IT companies established in Russia which was sold to the American F5 Networks in 2019.

## SNAPSHOT 10: IT RACKET - THE CASE OF NGINX

*Nginx*, a popular open-source web server used by over one third of the world's websites, was released by Igor Sysoev in 2004. In 2011, Sysoev, together with Maxim Konovalov, founded a company of the same name to provide support for its paid version, *Nginx Plus*. The company's clients included Facebook, Apple, Netflix, BuzzFeed, and Yandex, among others. In 2019, the *American F5 Networks* bought *Nginx* for \$670 million. Following this acquisition, the Moscow offices of *Nginx*, as well as Sysoev and Konovalov's homes were raided by the police. The *Nginx* founders were detained and interrogated, their mobile phones and computers were seized. The raid was connected to a copyright violation claim against *Nginx* by the *Rambler* Group. Their argument was that *Nginx* was developed while Sysoev was an employee of *Rambler* between 2001 and 2011. Yet, *Rambler* never ordered the server development, and was not even one of the *Nginx* first adopters. Sysoev worked on *Nginx* in his free time using his own computer, which was confirmed by *Rambler's* former chief executive and chief operating officers. Moreover, *Rambler* had never claimed ownership of *Nginx* in the 15-year period since its release.

According to Konovalov, "The big money [from the F5 Networks acquisition] became palpable, and then we see the desire [of *Rambler*] to grab a piece of it for themselves... It's a typical racket. Simple as that." The outraged tech community organized protests, with some websites staging a 30-minute blackout in support of the *Nginx* company. Eventually, *Rambler* had to drop the criminal case in Russia due to lack of evidence. This story, however, had a sequel in 2020 when Lynwood Investments, a Cypress-based holding company linked to the *Rambler* Group and Russia's billionaire Alexander Mamut, filed a lawsuit in the U.S. District Court for Northern California. It alleges that *F5 Networks*, the *Nginx* founders, some other former *Rambler* employees, and two venture capital firms that funded the startup conspired to steal *Nginx*. In its turn, *F5 Networks* states that they conducted a due-diligence of the *Nginx* company and are confident that *Rambler* has no rights whatsoever to the web server.<sup>57</sup>

<sup>56</sup> Bank of Russia (2021) Estimate of Key Aggregates of the Balance of Payments of the Russian Federation in 2020, [http://www.cbr.ru/eng/statistics/macro\\_itm/svs/bop-eval/](http://www.cbr.ru/eng/statistics/macro_itm/svs/bop-eval/), accessed January 29, 2021.

<sup>57</sup> "A Typical Racket, Simple as That" (2019) Meduza, December 13, <https://meduza.io/en/feature/2019/12/13/a-typical-racket-simple-as-that>, accessed February 16, 2021; Rapoza, K. (2020) "In Weird Twist, Russians Sue American Firms For IP Theft," *Forbes*, August 31.

**Russia's standing in international business rankings reflects these negative trends.** In 2019, Russia received 66.7 out of the maximum 100 points on the Global Competitiveness Index, with the weakest scores of 53 on the country's institutions, product market, and innovation capability.<sup>58</sup> In 2020, Russia ranked 129th out of 180 countries in Transparency

International's Corruption Perceptions Index.<sup>59</sup> A 2018 Pew Research Center study found that 59% of Russians believe that corrupt political leaders are a major concern for the country.<sup>60</sup> Ernst & Young's survey, conducted in 2020, found that foreign businesses in Russia consider administrative barriers (39%) and the mismatch between the law and current conditions (34%) as their key problems.<sup>61</sup>

Russia's case vividly shows that without secure property rights, the rule of law, and an independent judicial system, it is impossible to create a healthy business environment, attract domestic and foreign investors, expand high-tech industries, and diversify the economy out of its dependence on natural resources.

## THE OUTLOOK

**One of the most important trends in Russia that can be traced over the last three decades is the transformation of private reiderstvo that was typical of the 1990s into "state reiderstvo" since Putin's rise to power.**<sup>62</sup>

Starting from the early 2000s, public officials and security officers increasingly operate as aggressors and illegal raiders, instead of just facilitators and intermediaries of raiding attacks as in the 1990s. Primarily, state reiderstvo is associated with illegal raiding at the corporate level, so called "velvet re-privatization,"<sup>63</sup> meaning the redistribution process based on the abuse of the legal and judicial systems by high-ranking officials.

Through this process, Russia's political elites managed to regain control over the most profitable private businesses, primarily in the natural resource, oil, and gas sectors, as well as in financial, defense, and high-tech industries.<sup>64</sup> At the same time, as this report shows, small businesses and individual entrepreneurs often become victims of low-ranking and mid-level public officials and security officers.

**Starting from the 2008 economic crisis, Russia's political elite has made several attempts to centralize and limit low-ranking and mid-level corruption and illegal raiding.** These attempts include the 2010 package of anti-corruption laws, selective arrests

of corrupt officials, the creation of Russia's business ombudsman office, and the 2016 and 2020 temporary bans on regulatory inspections of small and mid-sized businesses. In 2016, President Putin also created a working group consisting of federal executives and business associations that together developed amendments to the Criminal Code to prevent unjustified criminal prosecution of entrepreneurs and illegal raiding. Although originally these attempts had some limited success,<sup>65</sup> both the number of entrepreneurial complaints about illegal raiding and the number of economic crime cases opened against businessman increased in the last years.

<sup>58</sup> World Economic Forum (2020) *Global Competitiveness Report*, <https://www.weforum.org/reports/how-to-end-a-decade-of-lost-productivity-growth>, accessed February 21, 2021.

<sup>59</sup> Transparency International (2021) *Corruption Perception Index 2020*, <https://www.transparency.org/en/cpi/2020>, accessed January 29, 2021.

<sup>60</sup> Pew Research Center (2018) "Russians Say Their Government did not Try to Influence U.S. Presidential Election", Washington, D.C., p. 3.

<sup>61</sup> Ernst&Young (2020) *The Outlook for International Business in Russia*, [https://www.ey.com/en\\_ru/news/2020/10/ey-fiac-survey-eng-2020](https://www.ey.com/en_ru/news/2020/10/ey-fiac-survey-eng-2020), accessed January 29, 2021.

<sup>62</sup> Rochlitz, M. (2014) "Corporate Raiding and the Role of the State in Russia," *Post-Soviet Affairs*, 30, 2-3, 89-114; Gans-Morse, J. (2012) "Threats to Property Rights in Russia: From Private Coercion to State Aggression," *Post-Soviet Affairs*, 28(3), 263-95.

<sup>63</sup> The term "velvet reprivatization" was coined by Oleg Shvartsman in 2007 in his interview with *Kommersant*, a Russian business newspaper, in which he referred to methods used by Putin's insiders to seize companies. Later, apparently under pressure, Shvartsman backed off of his statements and accused *Kommersant* of distortions of his words.

<sup>64</sup> Osipian, A. (2019) *Political and Economic Transition in Russia: Predatory Raiding, Privatization Reforms and Property Rights*, New York: Palgrave Macmillan.

<sup>65</sup> Rochlitz, M., Kazun A., and Yakovlev A. (2020) "Property Rights in Russia after 2009: From Business Capture to Centralized Corruption?" *Post-Soviet Affairs* 36, 5-6, 434-50.

**This illegal raiding pandemic continues amid COVID-19 business disruptions, which have exacerbated the problems of Russian entrepreneurs.** About 70% of small, medium-sized, and large enterprises were impacted by the COVID-19 pandemic, while only one third of them received government aid.<sup>66</sup> Amid

falling consumer demand, lockdowns, and COVID-19 restrictions, illegal raids and extortion by public agencies and officials created a double burden on enterprises. In the words of the Russian business ombudsman, “The policemen and investigators are simply finishing off the domestic business, which is already having a hard time.”<sup>67</sup>

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“The policemen and investigators are simply finishing off the domestic business, which is already having a hard time.”

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**Russia’s case provides strong evidence that random application of anti-corruption and anti-raiding measures, as well as selective protection mechanisms for raided businesses, cannot solve the systemic problems of illegal business raiding and corruption.** In Russia, there is a dire need to address the fundamental problems related to illegal business raiding, such as the absence of an independent judiciary, the abuse of law enforcement, outright repression of human rights and civil society, and suppression of press freedom. These critical challenges require structural reforms of the entire political and socioeconomic systems

in the country, as well as mobilization of Russian businesses in collective action to protect their rights and assets. Collective action could be a way for small businesses and entrepreneurs to leverage their influence and power to counteract corrupt public officials and illegal raiders. However, in order to be effective, entrepreneurial organizations in Russia should move away from their limited focus on the promotion of the interests of their members toward the use of open and direct mechanisms to represent the interests of the entire entrepreneurial community.

*Although reiderstvo*

*originates in Russia and other former Soviet states, its impact is global.* As this report shows, misuse of legal procedures in Western courts and arbitration bodies and abuse of international institutions such as Interpol represent important aspects of this problem. Even more damaging, perhaps, is the growing corrosive impact of dirty money from illegal raiding, corruption, and economic criminality on the global economy and Western democracies. This is why it is important to continue research efforts related to these new threats and challenges to democratic institutions in order to protect them from such abuses.

<sup>66</sup> “Pochti 70% rossiyskikh kompaniy postradali iz-za pandemii koronavirusa” [in Russian] (2020, May 28) RBK, <https://www.rbc.ru/economics/28/05/2020/5ecf711b9a7947324d-1448cf>, accessed February 10, 2021.

<sup>67</sup> “Titov rasskazal o ‘reyderskoy atake’ na biznes” [in Russian] (2016, September 16) Lenta.Ru, [https://lenta.ru/news/2016/09/16/siloviki\\_protiv\\_bisnesa/](https://lenta.ru/news/2016/09/16/siloviki_protiv_bisnesa/), accessed February 10, 2021.

