

CORRUPTION

BALTIC PRESCRIPTION FOR REMISSION



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No country in the world is free from corruption and the fight against it is key to the survival of any civilized state. The corruption report published by Transparency International this year provided corruption perception index for 2011 and put Russia on the 143th place out of 183. The situation in the Baltic countries is different: Estonia is ranked 29th, Lithuania - 50, and Latvia - 61. The index determines perception of public sector corruption in a country and is based on opinion polls of experts and businessmen.

It should be noted that Russia demonstrates a clear positive trend as the 2010 index placed it 154th out of 178. How can the improvement be explained? We believe it is due to the adoption of a package of anti-corruption laws which determine the main legal grounds to prevent public sector corruption and introduce responsibility also for bribing foreign and international officials. The legislation allowed Russia to state its readiness to join a number of international anti-corruption conventions. It can be stated at present that Russia has finally formed the legal and organizational basis to counteract corruption. It ratified several basic international agreements and adopted strategic and national anti-corruption plans to implement them.

Will that be enough? Hardly so. Statistical data confirm it. In particular, a report by Russian Prosecutor General Yuri Chaika on law and order in 2011 said over 312 thousand corruption offenses were exposed last year (38% increase).

CORPORATE CRIME IN RUSSIA

A major unresolved problem in Russia is the absence of criminal responsibility for legal entities for corruption crimes. It happens despite recommendations of the Group of States Against Corruption (GRECO). The recommendations demand to revise both legislative and traditional domestic approaches to legal grounds for criminal charges. Traditionally, legal entities cannot face legal charges and only individuals can be brought to responsibility for committed offenses.

However, the issue is being resolved. Head of the Russian Investigative Committee Alexander Bastykin said Russia had embarked on the modernization course which is impossible without streamlining existing economic relations specifically in attracting and investing private equity. The recent rapid growth of crimes committed through legal entities cannot but cause concern. The scope of the phenomenon is impressing and allows to state that Russia has got a new quality crime, i.e. of legal entities (which is called "corporate crime" or "corporation crime" abroad).

Russia is ready to join OECD Anti-Bribery Convention

The legal entity crime in Russia poses a real threat to economic security of the country and the interests of honest market players. In particular, it negatively affects Russian investment attractiveness (as it increases investment risks related to Russian financial instruments which are not protected from criminal infringements) and promotes capital outflow.

Criminal activities of legal entities destabilize the fundamental economic factors and thus indirectly facilitate the decline of major economic indicators. It is an explanation for growing inflation, falling production, and the exodus of capital to the shadow economy.

Rapid price hikes on major consumer goods in Russia are due not only to rising world

prices and other economic factors, but mostly to speculative deals and manipulated prices on the market of goods and services. Plus there is monopoly price fixing among dishonest companies which make super profits by shaking the basics of economic stability of the country.

And, finally, the criminal activity of some legal entities pushes up general crime in society and creates preconditions for such dangerous social phenomena, as corruption, environmental crime, terrorism financing, and organized crime.

The draft amendments to Russian legislation related to the introduction of criminal responsibility for legal entities have been published on the website of the Russian Investigative Committee.

BORROW EXPERIENCE FROM NEIGHBORS

It would be appropriate to examine the experience of Baltic countries. The Criminal Code of Lithuania adopted on September 26, 2000 states that both legal entities and private individuals can be charged. Legal entities bear responsibility for actions of individuals committed in the interests or for the benefit of a legal entity if they acted individually or upon instruction of the legal entity or if office duties of the individual allowed to act in the name of the entity,

adopt decisions on its behalf or control activities of the entity. Legal entity responsibility emerges also when an employee commits criminal offenses for the benefit of the given entity because of insufficient control of his or her actions. Thus, a Lithuanian legal entity is liable to responsibility for such corruption crimes, as bribery, graft, and money laundering.

Estonia has its own anti-corruption instruments. The republican Criminal Code came into force ten years ago and allows charging a legal entity for crime or offense.

Latvia does not stay aside either. Its Criminal Code says legal entities are liable to criminal responsibility. Punishment varies from fines, limitation of title or confiscation of property, and commitment to reimburse the damage completely. The Latvian code says responsibility for a crime shall be borne by the individual who com-

mitted the offense as a representative of a legal entity or upon its instruction, or during employment with the legal entity, or as an accomplice of the legal entity.

In a word, foreign experience shows it is necessary to combine various anti-corruption measures.

REFORM THE LEGISLATION

To efficiently qualify offenses committed by Russian legal entities it is necessary to consider changes to civilian legislation because of the blanket character of current norms. In particular, the



draft amendments to Parts 1, 2, and 3 of the Civil Code of the Russian Federation contain article 53.1 which envisages responsibility of an individual authorized to act on behalf of a legal entity, its board and decision-making officials.

It says an individual authorized to act on behalf of a legal entity due to the force of law or normative act or charter of the entity or on other grounds shall reimburse losses inflicted to the legal entity upon a demand of the entity and its founders (participants). The individual will bear

responsibility if it is proved that he has acted dishonestly while exercising his rights and duties or his actions (inaction) breached the usual civilian or normal entrepreneurial risk norms. However if he acted honestly, board members of the legal entity, excluding those who voted against the detrimental decision or were absent during the vote, will face responsibility.

In a word, we can say the civil law plans to introduce responsibility for board members of a legal entity which allows to charge them with complicity in crimes committed by legal entities.

It is important that the draft federal law defines a legal entity as an organization with its own property

which is subject to debt liabilities, with the right to enjoy and exercise civil rights and bear civil responsibilities, be a plaintiff and defendant in court.

It is important the lawbill stipulates that by contributing to the property of a legal entity the founders hold obligatory title to the legal entity or material rights to its property.

These were the tasks set for the Concept of the development of civil legislation in the Russian Federation approved by the Council for codification and streamlining of civil legislation at the Russian

president. It envisages obligatory subsidiary liability of various individuals, mostly the founders of a legal entity, for its debts. It would be difficult to argue that Article 56 of the Civil Code should not contain additional provision on subsidiary property liability of guilty founders, participants, beneficiaries and other individuals who have the decisive say in decisions and deals adopted by the legal entity with counteragents.

The same concerns criminal responsibility of the founders, participants, beneficiaries and other individuals who have the decisive say in deals of the legal entity. What is the situation now? It often happens that documents of a legal entity are issued to a frontman. Therefore, there should be criminal responsibility not only for managers, but also for founders. It will make those people who agree to share the fate of director Funt from Ilf and Petrov's novel about Ostap Bender think well and realize they can face criminal charges for offenses committed by the company which they formally created.

It is still not enough. Another criminal measure shall be stipulated. The mentioned draft says a court can sentence a legal entity involved in an offense to one or several punishments: a) warning, b) fine, c) cancellation of license, quotas, preferences and privileges, d) ban on certain type of activities, e) ban on operations in Russia, f) forced liquidation.

To compare: in Lithuania punishment for a legal entity may include a fine, title restriction, property confiscation, damage reimbursement, and liquidation. In Latvia - liquidation of the legal entity, title restriction, property confiscation, monetary fine. Additional enforcement measures envisage property confiscation and damage reimbursement.

The criminal punishment stipulated by the Russian lawbill - ban on certain types of activities - is identical to the punishment stipulated by the Russian Criminal Code - ban on certain activities. The lawmakers have either to unify the wording or provide interpretations for each provisions and explain the difference.

Article 47 of the Russian Criminal Code explains that the ban on certain activities means a ban on concrete professional or other activi-

ties. The criminal law describes professional activities as permanent employment that demands special knowledge or training (medical staff, teachers, lecturers, accountants, lawyers, attorneys, etc.). Other relatively permanent activities related to fishing, hunting, medicinal herb collection, etc. are not included.

Thus, the criminal punishment stipulated in the lawbill as "ban on certain types of activities" differs from that in Article 47 of the Russian Criminal Code. One can differently interpret a ban on certain types of activities - either a prohibition to

Efficient foreign experience shows it is necessary to combine various anti-corruption measures. Why shouldn't Russia follow suit?

engage in certain activities (trade, construction, securities) or prohibition to act as a founder, participant, and beneficiary of a legal entity.

We believe it is important to use the "principle of identification" for the crime committed by a legal entity. In this case, if a court finds a legal entity involved in a crime the sentence has to list concrete type of activity which the guilty side is banned to perform. It is evident that a ban on participation in a legal entity would be serious punishment for a founder, participant, and beneficiary. It is specifically important in Russia where legal entities can be easily set up. The ban may stop individuals from intention to act as a frontman posing for the founder of a legal entity.

It would be appropriate to include in Article 44 "Types of Punishment" of the Russian Criminal Code a "ban on the right to occupy management and governing positions in a legal entity and be its founder or stakeholder."

The Concept of the development of Russian civil legislation stipulates no specific legal competence for offshore-registered foreign entities, i.e. in foreign tax havens which do not demand disclosure of information on financial transactions. However offshore companies are often used for civil law abuse (creation of a faked honest beneficiary, concealing unlawful manipulations with shares, forcible takeovers, etc.).

Isn't it appropriate to discuss a possibility of introducing into Russian legislation an additional term for legal competence of offshore

companies - their registration in the single state register of legal entities with obligatory disclosure of information about the founders (participants) and beneficiaries? Only such registration and disclosure would allow offshore companies to operate on the Russian territory, execute deals, acquire property, etc.

However, the provision was not included into the draft federal law on amending parts 1, 2, and 3 of the Russian Civil Code and other laws of the Russian Federation. We believe it is wrong. Legal entities with foreign equity registered offshore shall face equal criminal and legal responsibility with other legal entities.

There are high-profile examples of corruption crimes committed by foreign legal entities. The media reported numerous offenses which official authorities did not deny.

PRICE TAG

In 2003 IKEA built its first distribution center in Russia - a warehouse in Solnechnogorsk near Moscow (\$40 million investment). The first director of IKEA Mos, Lennart Dalgren, said he received an oral permission from Solnechnogorsk district chief, Mr. Popov, for the construction.

"All of a sudden police arrived to the construction site. All work was stopped, access denied and we could not enter the territory", Dalgren recalled.



He tried to contact Popov, but in vain. Some time later he emerged from nowhere and promised to resume construction permission if IKEA pays 10 million rubles.

Dalgren said: "OK, we shall pay but on one condition: the money will go to nursing homes. I had a feeling we have agreed, but two days later Popov came and said the deal is terminated. He said 30 million rubles are to be paid. We were losing thousands of dollars each idle day and it was cheaper to pay 30 million."

IKEA remitted the money to a charity fund and informed the city and media about it. "Police left and construction resumed," Dalgren said.

A similar story happened to Mega Khimki a year later. The startup of a shopping mall

scheduled for December 2004 did not take place as Gosarkhstroiadzor watchdog did not sign a state acceptance act because the mall was using standby electricity generators and no traffic interchange was built. IKEA had to build two bridges worth \$4 million each (one has not been commissioned yet) and promise \$1 million for the development of children's sports.

Director General of "Colliers International - Russia" Mr. Gasiev said state regulation of construction industry encourages bribery.

None of the polled market participants and experts agreed to estimate the total amount of bribes and name himself. Anonymously they provided similar figures: if a company is constructing without any permission at all the kickback for documents after commissioning may reach 30% of construction costs and 20-30 percent for electricity provision.

A top official of Management Development Group said "nobody has been giving bribes in cash for long, everything is arranged as social support or a part of construction is given to subcontractors named by local officials." The IKEA experience in Solnechnogorsk shows the appetite of officials is not always too big. In 2004 Yekaterinburg local administration demanded IKEA to pay 10% of projected costs (\$150 million) to "voluntary funds" for city infrastructure development.

CONCLUSIONS

By analyzing these and other cases we concluded it is necessary to design measures also for foreign legal entities.

For example, laws shall stipulate that executive duties in a foreign legal entity are performed by a sole executive body (legal entity chief), member of the governing board, member of the council of directors, or another individual who permanently or temporarily performs executive or administrative duties in a legal entity according to a special authorization. An



individual who actually governs a foreign legal entity shall be a person who may not occupy any position in the management of the entity and possess no powers according to the law, charter and contract or a power of attorney to manage, administer and execute decisions in the legal entity, but who determines the decisions adopted by the legal entity due to his dominating stake in the authorized capital or due to other circumstances.

There is yet another important issue. It is necessary to legislatively determine types of crimes to which a legal entity can be liable. It would be proper to recollect that according to Article 10 Liability of legal persons of the United Nations Convention against Transnational Organized Crime adopted by the 55th session of the UN general Assembly, "each State Party shall adopt such measures as may be necessary, consistent with its legal principles, to establish the liability of legal persons for participation in serious crimes involving an organized criminal group and for the offences established in accordance with articles 5, 6, 8 and 23 of this Convention."

A question arises in this connection: why shouldn't we use in anti-corruption fight the experience accumulated due to the Instruction of the office of the Russian prosecutor general № 52-11 and of the Russian interior ministry № 2 of 15.02.2012 on Introduction of a list of articles of the Russian Criminal Code for the provision of statistical reporting? It lists № 13 crimes that can be committed through office abuse or in selfish interests by officials, state servants, and local self-government officials, as well as executive officers in a commercial or other company, as well as offenses that can promote the crimes.

If there are concerns about enhanced efficiency and prevention of law enforcement problems while introducing criminal responsibility for legal entities we suggest to use the rich experience of our close neighbors - Estonia, Lithuania, and Latvia.