

2008

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Recommended Citation

Thomas Firestone, *Criminal Corporate Raiding in Russia*, 42 INT'L L. 1207 (2008)
<https://scholar.smu.edu/til/vol42/iss4/2>

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Criminal Corporate Raiding in Russia

THOMAS FIRESTONE*

I. Introduction

The illegal takeover of businesses, commonly known in Russian as “reiderstvo” (raiding), has become a major threat to domestic and foreign investors in Russia. “Reiderstvo” differs greatly from U.S. hostile takeover practice in that it relies on criminal methods such as fraud, blackmail, obstruction of justice, and actual and threatened physical violence. At the same time, though, “reiderstvo” is not just simple thuggery. In contrast to more primitive criminals, Russian “reideri” rely on court orders, resolutions of shareholders and boards of directors, lawsuits, bankruptcy proceedings, and other ostensibly “legal” means as a cover for their criminal activity. “Reiderstvo” is also more ambitious than classic protection schemes in that it seeks not just a portion of the target business’ profits but the entire business itself. Finally, because raiding typically involves the use of documents such as corporate resolutions and judicial orders as covers for threats of physical violence, it is more sophisticated and can be much more difficult to investigate and prosecute than straightforward extortion schemes. In short, it is a new and sophisticated form of organized crime.¹

There is growing recognition that corporate raiding has become one of the biggest criminal problems in Russia. According to statistics compiled by the Ministry of Internal Affairs (“MVD”), raiding generates approximately 120 billion rubles (over \$40 million) a year in illegal profits, and, considering that this statistic is based only on the rare cases actually investigated by the MVD, the true amount is certainly far higher.² Ivan Novitskii, a deputy of Moscow City Duma (a municipal legislative body in Moscow), claims that 300 Moscow businesses are raided every year and that thousands more are at risk.³ In a recent study by Price Waterhouse, businesses operating in Russia identified “asset misappropriation” as the most common type of corporate crime.

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1. Perhaps the closest historical analogy is the phenomenon of Japanese *sokaiya*, professional criminals who exploit their status as corporate shareholders in order to extort money from the corporation. See, e.g., KENNETH SZYMKOWIAK, *SOKAIYA: EXTORTION, PROTECTION AND THE JAPANESE CORPORATION* (East Gate Books 2002) (2001).

2. PAVEL ASTAKHOV, *PROTIVODEISTVIYE REIDERSKIM ZAKHVATAM 5-6* (Eksmo 2007) [hereinafter *ASTAKHOV-PROTIVODEISTVIYE*].

3. Ivan Novitskii, *Tezisy doklada deputata Moskovskoi gorodskoi dumy* (Nov. 16, 2007) (unpublished manuscript, presented at roundtable on raiding, Moscow Oblast Advocates Chamber, on file with author).

tion" as their top criminal problem.⁴ Businesses of all sizes, from the smallest to the largest, have been victimized. The prevalence of raiding is also demonstrated by its popularity as a subject for television and movie dramas, while bookstores are full of manuals on how to protect business against illegal raids.⁵

There is growing recognition, too, that corporate criminal raiding also presents a serious threat to the Russian economy. It deters business development and undermines investor confidence. President Medvedev has called raiding "shameful" and noted its stifling effect on Russian business.⁶ Raiding also poses a serious threat to foreign investors. William Browder, manager of Hermitage Capital Management hedge fund, one of Russia's largest foreign investors, recently claimed that raiders stole several of Hermitage's investment vehicles by falsifying corporate documents and filing frivolous lawsuits as part of a \$230 million fraud scheme.⁷ British Petroleum (BP) Chairman Peter Sutherland claimed that the BP half of a joint venture with the Russian oil company TNK has also been the victim of a corporate raid.⁸

Raiding also affects foreign investors in another, less obvious way. Alleging corruption in Russian courts, victims of Russian raids have begun to seek redress in U.S. courts. Complaints alleging raiding in the metal and oil industries have been filed in U.S. district courts.⁹ One U.S. lawyer has even developed a specialization in bringing U.S. suits arising out of alleged raids in Russia.¹⁰ It should be noted, however, that these cases have all been dismissed on *forum non conveniens* grounds.

4. Survey, PRICE WATERHOUSE COOPERS, ECONOMIC CRIME: PEOPLE, CULTURE AND CONTROLS, THE 4TH BIENNIAL GLOBAL ECONOMIC CRIME SURVEY: RUSSIA 3 (2007).

5. See, e.g., *Okhota Na Izyubrya*, (Pervaya Videokampaniya, 2005) (12 episode television mini-series based on popular novel of the same name about takeover of a steel plant in Siberia); PAVEL ASTAKHOV, REIDER (Eksmo 2007) (popular novel about criminal takeover of industrial research institute) [hereinafter ASTAKHOV-REIDER]; SERGEI SERGEEV, ANTI-REIDER (OLMA Media Grupp 2008) (novel about oligarchs raiding a multi-million dollar business through judicial corruption, industrial espionage, commissioned tax inspections, and other illegal means).

6. See, e.g., INFORMATION AGENCY, MEDVEDEV: ZA REIDERSTVO NUZHNO BIT' PO RUKAM (Feb. 27, 2008), <http://www.rosbaltvolga.ru/print/460264.html>; Philip Aldrick, *Exposing Russia's Corporate Corruption*, THE DAILY TELEGRAPH, May 4, 2008, www.telegraph.co.uk/money/main.jhtml?xml=/Money/2008/04/04/ccrussia104.

7. Aldrick, *supra* note 6; Carl Mortished, *Hermitage Capital Alleges Fraud and Theft Involving Russian Interior Ministry*, TIMES ONLINE, Apr. 4, 2008, http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article3678222.ece; Carl Mortished, *Bill Browder at Home after Mean Streets of Moscow*, TIMES ONLINE, Aug. 4, 2008, http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article4453893.ece.

8. Johan Carlstrom & Lyubov Pronina, *BP Vents Frustration over Russian 'Corporate Raiding'*, INDEPENDENT, June 13, 2008, <http://www.independent.ie/business/european/bp-vents-frustration-over-russian-corporate-raiding-1407959.html>.

9. See, e.g., *Base Metal Trading Ltd. v. Russian Aluminum*, 253 F. Supp. 2d 681, 682 (S.D.N.Y. 2003) (plaintiffs alleged that a consortium of companies took control of the Russian aluminum and vanadium producers through a pattern of racketeering activity, including bribery, judicial corruption, sham bankruptcy proceedings, and armed force); *Davis Intern., LLC v. New Start Group Corp.*, 488 F.3d 597, 598 (3d Cir. 2007) (plaintiff majority shareholders of Russian vanadium company claimed that defendants had taken control of company through a pattern of racketeering activity); *Norex Petroleum Ltd. v. Access Indus., Inc.*, 304 F. Supp. 2d 570, 570 (S.D.N.Y. 2004) (Canadian oil corporation sued various corporations and individuals alleging that massive racketeering and money laundering scheme was orchestrated to take control of Russian oil industry).

10. Nathan Vardi, *Justice, Russian Style*, FORBES, Mar. 24, 2008, <http://www.forbes.com/business/forbes/2008/0324/144.html>.

Raiding is so widespread that Russia has even spawned a class of professional raiders.¹¹ Some of them operate as “consultants” who, for a fee, help clients plan and execute illegal takeovers of target companies.¹² In 2005, one alleged raider, who has never been charged or convicted for raiding, published an article on his website explaining how to take over a business and listing the prices he charged for various services, including: assessing a target’s capacity to resist an attack (\$3,000 to \$10,000); altering a target company’s corporate register (starting at \$10,000 in Moscow and \$1,000 in the regions); and initiating a criminal case against a target (starting at \$50,000 in Moscow and \$20,000 in the regions outside Moscow).¹³ One researcher recently conducted an anonymous survey of raiders and identified the following standard prices in Moscow (prices outside Moscow are less) for the following services:

- altering a target company’s corporate documents: 10,000 euros and up;
- notarizing documents: from 3,000 to 10,000 euros;
- obtaining a court ruling: from 30,000 to 200,000 euros;
- “neutralizing” of police and prosecutors: from 30,000 to 60,000 euros;
- effecting a forcible seizure of a business: 300.00 to 500.00 euros for each armed attacker.¹⁴

Despite the serious, widespread nature of this problem, there has been little analysis of it in the United States. This article attempts to fill that gap. It analyzes, first, the tactics used by raiders; second, the underlying causes of raiding; and third, some of the gaps in Russian law that make raiding possible. It concludes with some recommendations about what Russian authorities can do to alleviate the problem and how businesses can protect themselves.

II. Background on Corporate Raiding

A. SCHEMES

Although Russian analysts have repeatedly tried to classify the schemes used by raiders, the analysts’ work demonstrates that raiders use ever-changing combinations of various techniques, none of which are mutually exclusive, making a neat typology impossible.¹⁵ For analytical purposes, it is simplest to say that most raids use a basic scheme augmented by supplementary tactics. A review of the available literature suggests that four basic schemes—which we will label (a) bankruptcy, (b) corporate, (c) litigation, and (d) land schemes—appear to be the most widespread. We will examine each of these and then examine the various supplementary tactics that are typically used to support the basic schemes.

11. MAKSIM IONTSEV, KORPORATIVNIYE ZAKHIVATI 38 (2d ed., Os’-89 2008); Novitskii, *supra* note 3, at 3.

12. IONTSEV, *supra* note 11, at 38.

13. Vladimir Solovyov, Iskrenne Vash, E.O., *Stoimost’ organizatsii zakbuvata reideri otsenivayut primerno kak ustroyennuyu stoimost’ natural’nykh raskhodov v sootvetstviy so smetoi*, Sept. 21, 2005, <http://www.compromat.ru/main/luzkhov/olevinskij2.htm>.

14. DMITRY ZERKALOV, REIDERI 97 (2007).

15. See, e.g., IONTSEV, *supra* note 11; ZERKALOV, *supra* note 14.

1. *Bankruptcy Schemes*

In bankruptcy schemes, the raiding company typically acquires a substantial portion of the target company's debt, forces the target company into bankruptcy by demanding immediate repayment of the debt, and then corruptly obtains control over and manipulates the bankruptcy proceedings to take complete control of the target company.¹⁶ As one analyst has explained, these bankruptcy schemes typically proceed in five stages.¹⁷ First, the raider, usually a corporate entity, acquires information on the target company's debts and finances. Second, the raider covertly acquires the target company's debt either alone or through an alliance with an existing creditor. Third, the target company goes into bankruptcy proceedings controlled by a manager or trustee who has been selected by, or is corruptly influenced by, the raider. Fourth, the raider obtains a judgment authorizing it to take the target company's assets. Finally, the raider "enforces" the judgment and physically takes control of the company, usually through an armed assault.¹⁸

The plaintiffs' allegations¹⁹ in the *Base Metals* case provide a good example of such a scheme. According to the complaint, the defendants, working through a corrupt regional governor in Tyumen, obtained an arbitrazh court judgment against the target enterprise in the amount of \$26.3 million.²⁰ Using this judgment, they put the target into bankruptcy and arranged to have one of their confederates appointed as Provisional Bankruptcy Manager.²¹ The manager then recognized an additional \$70 million worth of fraudulent claims brought against the target company held by other companies also controlled by the raiders.²² Recognition of these fraudulent claims gave the defendants majority voting power at subsequent creditors' meetings, which they used to effectuate the complete take-over of the target enterprise.²³

Bankruptcy raids were most common between 1998 and 2002 because a liberal bankruptcy law then in place made it easy for small creditors to force debtors into bankruptcy.²⁴ Under the prior (1992) bankruptcy law, a debtor company could go into bankruptcy only if its total debts exceeded its total assets, thus making bankruptcy unduly difficult.²⁵ The law was changed in 1998 to allow any creditor who held a debt of 500 times the monthly minimum wage (approximately \$5,000 in 2002) that remained unpaid

16. *Base Metal*, 253 F. Supp. 2d at 683 (plaintiffs alleged that defendants drove target companies into bankruptcy and then gained control of the companies through sham bankruptcy proceedings overseen by allegedly corrupt local Russian judges); ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 34.

17. Vadim Volkov, *Hostile Enterprise Takeovers: Russia's Economy in 1998-2002*, 29 REV. OF CENT. & E. EUR. L. 527, 533-34 (2004).

18. *Id.*

19. For reasons set forth below, there are very few convictions of raiders in Russia. Therefore, in discussing particular cases, this article relies heavily on publicly available allegations by victims and law enforcement. Unless otherwise noted, nothing in this article should be taken as a statement by the author or the U.S. government that the individuals or companies mentioned as defendants or subjects in raiding cases are in fact guilty or that they should not be presumed innocent.

20. *Base Metals*, 253 F.Supp. 2d at 687.

21. *Id.*

22. *Id.* at 688.

23. *Id.*

24. For example, much of the *Base Metals* bankruptcy scheme is alleged to have taken place during this period.

25. LEONARD BIERMAN & YURI FEDOTOV, *BANKRUPTCY IN RUSSIA* (Jan. 5, 2002), http://www.gsom.pu.ru/files/en/upload/research/06_Bankruptcy_IN_Russia.pdf.

for three months to file a demand for bankruptcy and obtain the appointment of a temporary manager.²⁶

As one expert wrote, "[t]he [1998] law on bankruptcy was simply created for raiders."²⁷ Sidney Brooks, a U.S. Bankruptcy Court Judge in the District of Colorado who participated in drafting corrective amendments to the 1998 law wrote that the "streamlined, drive-through" procedures provided for in the 1998 law were "a formula for great mischief."²⁸ According to Vadim Volkov in his work "Hostile Enterprise Takeovers", approximately 30 percent of the bankruptcy cases adjudicated between 2000 and 2002 involved "contract bankruptcies" (*i.e.*, those corruptly orchestrated by raiders) to facilitate hostile takeovers.²⁹ Analysts claimed that temporary managers were frequently corrupted and helped raiders seize target companies.³⁰ In fact, according to one expert, debtors often were not even notified of the meeting at which the manager was selected; instead, raiders frequently sent an empty envelope to the debtors and then used the empty envelope in court as evidence that notification had been delivered.³¹

In order to address these problems, the new 2002 bankruptcy law imposed more stringent screening and ethical requirements for trustees, expanded the time for judges to consider and take decisions, and also expanded debtors' rights to contest creditors' petitions.³² The 2002 revisions made bankruptcy raids much more difficult by impeding raiders' ability to quickly force a company into bankruptcy proceedings and succeed in obtaining the appointment of a corrupt trustee.³³ As a result, bankruptcy raids decreased. According to one expert, after the 2002 revisions, all the raiders who formerly used the law on bankruptcy switched tactics and began to use loopholes in the corporate law.³⁴

2. Corporate Schemes

Corporate raiding schemes involve the corrupt acquisition of control over the target company usually by falsifying internal corporate documents and/or corruptly obtaining control over a significant portion of the voting stock or the board of directors of the target company. In one of the simplest schemes, the raider creates a false power of attorney or other document authorizing him or a co-conspirator to enter into transactions on behalf of the target company and then transfers the target's assets to himself or affiliated companies. In another, the raider bribes officials at state registration agencies to alter the target

26. *Id.* at 6.

27. Vladimir Ovchinskii, *Reideromafiya*, OGONYOK, Apr. 16-22, 2007, <http://www.ogoniok.com/4992/2/>.

28. Sidney Brooks, *Three's a Charm? Russia Adopts Third Bankruptcy Law in 10 Years*, AM. BANKR. INST. J., June 2002, available at http://findarticles.com/p/articles/mi_qa5370/is_200206/ai_n21314296/print?tag=artBody;coll.

29. Volkov, *supra* note 17, at 528.

30. William Thompson, *Reforming Russian Bankruptcy Law*, PROSPECTS FOR THE RUSSIAN FEDERATION PROJECT 2 (The Royal Institute for International Affairs Aug. 2004), available at <http://www.isn.ethz.ch/isn/Current-Affairs/Policy-Briefs/Detail/?lng=en&id=23044> ("All too often, administrators work to ensure that proceedings take the course desired by the specific creditors they serve, at times driving perfectly viable firms into liquidation.").

31. Volkov, *supra* note 17, at 533 n.11.

32. Brooks, *supra* note 28, at 1-2.

33. See *e.g.*, IONTSEV, *supra* note 11.

34. Ovchinskii, *supra* note 27, at 20.

company's registration documents to give him and/or his confederates faux control over the target company. He then uses this control to siphon out the target's assets.

In another scheme, the raider obtains a judicial order directing the target company to turn over the shareholder register to an entity or individual under the raider's control and then alters the register to put in place a false board of directors that transfers the assets to other companies the raider controls. A variation on this scheme involves the creation of a parallel shareholder register that falsely indicates a majority stake held by individuals and entities friendly to the raiders. This majority stake is then used to elect a new board of directors, which, in turn, transfers the target's assets to companies controlled by the raider.³⁵ In a similar scheme, raiders call a shareholders' meeting but fail to provide other shareholders adequate and timely notice, either by mailing notices to the wrong address, sending the notices only a short time before the meeting, or holding the meeting in a remote, inaccessible location. At the meeting, they exploit the artificially created majority to vote in a new board of directors.³⁶ Another scheme involves filing a frivolous lawsuit in order to obtain a court judgment temporarily restricting the voting power of other shares, thus giving the raiders a temporary majority, which they then use to change the board of directors.³⁷ Once the raiders gain a temporary majority, they make a supplementary stock issue in order to dilute the percentage held by the other shareholders and solidify the raiders' hold on the company.³⁸

In almost all of these schemes, the target company's assets, once acquired by the raiders, are rapidly transferred through one or more shell companies to an ostensible good faith purchaser.³⁹ By the time the scheme has been unraveled and adjudicated in court, the shell companies have disappeared, and the assets are safely in the hands of a party claiming to be a good faith purchaser, making it almost impossible to recover them. Thus, the raid has been successfully accomplished.

The Russian press is full of accounts of raids allegedly using such tactics. For example, in a major prosecution currently underway in St. Petersburg, reputed organized crime figure Vladimir Barsukov (also known by the criminal nickname, "Kumarin") is accused of having managed a raiding gang that attempted to raid over forty businesses.⁴⁰ According to investigators, the gang used corrupt connections to the tax police and the federal registration service to obtain access to the target companies' incorporation documents in the Unified State Corporate Register. The raiders then allegedly falsified the companies' registration documents to identify their co-conspirators as the actual owners and used this false control to transfer the companies' assets through a series of shell companies to other companies that the raiders controlled. Ultimately, again, a final transfer was made to an alleged good faith purchaser.⁴¹

35. ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 42.

36. ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 55; interview with Sergey Golkin, Investigator, Investigative Committee of the General Procuracy of the Russian Federation, in Moscow, Russ. (April 2008).

37. Volkov, *supra* note 17, at 536.

38. IONTSEV, *supra* note 11, at 71.

39. IONTSEV, *supra* note 11, at 77; ASTAKHOV-REIDER, *supra* note 5, at 66.

40. *Delo piterskikh reiderov*, LENINGRADSKAYA PRAVDA (Sept. 3, 2007), <http://www.lenpravda.ru/digest/spb/258310.html>.

41. See, e.g., Nina Volodina, *Proishestviya: Restoran okazalsya ne po zubam*, GAZETA, Aug. 17, 2008, <http://gzt.ru/incident/2008/08/17/223016.html>; *Delo predprinimatelya B. Barsukova (Kumarina), obvinyayemogo v*

In the Hermitage Capital case, the victim's principals and lawyers alleged that raiders orchestrated an MVD search of the offices of Hermitage Capital, one of the largest foreign investment funds in Russia. During the search, MVD agents seized corporate seals and other internal corporate documents of certain Hermitage investment vehicles. The seals and documents were then used to create false documents fraudulently showing that the companies were owned by people in league with the raiders. In a twist on traditional raiding schemes, the raiders then allegedly encumbered the stolen companies with fictitious liabilities, which they then used to obtain a \$230 million tax refund from the Russian government.⁴²

Similarly, the so-called Frukun case involved the allegedly illegal seizure of the largest warehouse and storage company in St. Petersburg. According to the putative victims, Frukun's 1,230 shares were originally held by members of the company's "labor collective." When the General Director of the company became ill, his Deputy became Acting General Director and formed a contract with a third party to manage the register of corporate shareholders. Pursuant to this contract, the register was turned over to the third party, and, during this process, many of the most important internal documents were mysteriously "lost." The Acting General Director and his partner then authorized a supplementary stock issuance and sold the newly issued shares to front purchasers who immediately sold them back to the Acting General Director and his partner.⁴³

3. *Litigation Schemes*

In a litigation scheme, the raider files one or more civil lawsuits against the target, often in a remote location where the raider has influence over the local judiciary, and then obtains a judicial order authorizing seizure of some or all of the target's assets.⁴⁴ This tactic was allegedly used in the much publicized Ilim Pulp case that involved an attempted (unsuccessful) raid of Ilim Pulp, Russia's largest forest products company, by a company controlled by oligarch Oleg Deripaska. In 2002, a minority shareholder in one of Ilim's mills filed suit in a remote location in Siberia, alleging that Ilim had failed to comply with all the terms of its 1994 privatization.⁴⁵ A judge awarded the plaintiff \$113 million in damages, confiscated two thirds of the mill's stock, and transferred the stock to the St. Petersburg State Property Committee, which then sold the stock to Deripaska and his partner.⁴⁶ Though Deripaska claimed that notice had been sent by mail, Ilim Pulp's owners claimed that they were never notified of the suit.⁴⁷ The Deripaska companies then sent in a private security force to seize the mill, and court bailiffs arrived with an order installing a new director.⁴⁸ The mill's owners, however, refused to yield and filed several

moshenichestve, peredano po podsumnosti v drugoi sud, RBC NEWS, Aug. 15, 2008, <http://spb.rbc.ru/freenews/20080815145942.shtml>.

42. Aldrick, *supra* note 6; Mortished, *supra* note 7.

43. *Udasty li vernut' "Frukun?"*, UTRO PETERBURGA (Mar. 30, 2006), <http://www.utrospb.ru/article/1642>.

44. Novitskii, *supra* note 3, at 7.

45. Daniel J. McCarthy & Sheila M. Puffer, *Pulp Battles a Hostile Takeover*, in *CORPORATE GOVERNANCE IN RUSSIA* 304 (Daniel J. McCarthy, Sheila M. Puffer, Stanislav V. Shekshnia eds., Edward Elgar Publishing 2004); Sabrina Tavernise, *Handful of Corporate Raiders Transform Russia's Economy*, N.Y. TIMES, Aug. 13, 2002, at A1.

46. Tavernise, *supra* note 45.

47. *Id.*

48. *Id.*

countersuits against the Deripaska companies.⁴⁹ Eventually, according to Deripaska, the case was settled amicably out of court.⁵⁰

A litigation tactic was also allegedly used in a shareholder dispute within the telecommunications company VimpelCom. The dispute involved shareholders Telenor, a Norwegian telecommunications company, and Alfa Group, a Russian investment group. In the VimpelCom case, Farimex—a tiny Virgin Islands company that owned less than 1 percent of VimpelCom—filed suit against Telenor in a remote court in Siberia, a location that had no discernible connection to the case. Nevertheless, the Siberian court (at 2:00 a.m. on a Saturday) handed down a \$2.8 billion damage award on behalf of Farimex.⁵¹

4. Land Schemes

Land raiding schemes are similar to corporate schemes in that they also often rely on the falsification of documents. Instead of falsifying internal corporate documents, however, the raiders falsify documents establishing title to pieces of real property. In a 2005 case in Moscow, a real estate developer was convicted of creating false documents purporting to establish ownership of 400 hectares of land, worth 6.5 million rubles.⁵² Another notorious alleged case of land raiding is the Boyko case. The lead defendant, Vasilii Boyko, and several employees of his company, Your Financial Advisor, are accused of having created false documents giving title to more than 35,000 square meters of valuable suburban Moscow land to companies under their control for the purpose of constructing an exclusive resort community.⁵³ Boyko claims that all of the land was acquired legally and that the charges against him have been fabricated by his enemies in order to sabotage his business.

Land raids are also facilitated by the uncertainty of property rights created by the privatization of state-owned farms in the early 1990s. Because the legal basis for so much of the privatization of state assets after the collapse of the Soviet Union was so vague, almost any property is subject to a challenge that it was illegally acquired. As Dmitri Larionov, the director of Peasant Front, an organization dedicated to protecting landowners against raids, said, "I can find a legal flaw in any privatization deal."⁵⁴ Given these uncertainties, big real estate developers and their high-powered lawyers often easily outmaneuver rural landowners, who lack in legal sophistication and the means to hire expensive lawyers.⁵⁵

49. McCarthy & Puffer, *supra* note 45, at 305; Tavernise, *supra* note 45.

50. Hugo Miller & Yuriy Humber, *Determined Deripaska Casts a Long Shadow*, ST. PETERSBURG TIMES, Apr. 29, 2008, http://www.sptimes.ru/index.php?story_id=25836&action_id=2.

51. See, e.g., Dan Sabbagh, *Telenor to Fight Siberian Court Order*, TIMES ONLINE, Aug. 18, 2008, http://business.timesonline.co.uk/tol/business/industry_sectors/telecoms/article4553417.ece; Martin Tomkinosn & Ben Laurance, *Norwegians Accuse Russians of Dirty Tricks in Telecoms Venture*, TIMES ONLINE, Nov. 25, 2007, http://business.timesonline.co.uk/tol/business/industry_sectors/telecoms/article2935757.ece.

52. Denis Tykulov, *Dom: Prokuratura proveryaet skupschikov podmaskovnykh zemel'*, GAZETA, Dec. 19, 2005, <http://gzt.ru/print.php?p=home/2005/12/19/211137.html>.

53. Kazim Baibanov, "Ruzskaya Shveitsariya" popolnilas' "Alfa Kapitalom", GAZETA RU: OBSHESTVO, Oct. 19, 2007, www.gazeta.ru/social/2007/10/19/2251074.shtml.

54. Interview with Dmitriy Larionov, leader, "Peasant Front" public movement, in Moscow, Russ., (Apr. 2008).

55. Vladislav Goncharuk, *Poseyanniye milliardy*, NOVAYA GAZETA, Sept. 11, 2006, <http://2006.novayaga-zeta.ru/nomer/2006/59n/n59n-s22.shtml>.

Faced with legal challenges to their property rights, these rural landowners often sell to the raiders at bargain prices rather than face the uncertain prospects of litigation.⁵⁶

5. *Supplementary Tactics*

In addition to the techniques described above, raiders typically use various supplementary tactics. A raider's first step is usually to obtain information about the victim firm in order to identify its attractiveness and vulnerabilities. Collection of information can take many forms, including requests by minority shareholders (usually front men who have recently purchased stock just for this purpose) for internal corporate information: the shareholders' register, tax information, information about the target's board of directors, and so on.⁵⁷ Information can also be acquired by purchasing it from law enforcement and regulatory authorities who have acquired it in the course of regulatory inspections (*proverka*) of the subject business. According to one report, 130 criminal cases have been opened against law enforcement officials for illegal selling of information obtained through regulatory inspections.⁵⁸ There have also been reports of raiders posing as representatives of official departments responsible for the protection of small and medium sized businesses calling the target and asking for information about its organizational structure, finances, and other aspects of its business.⁵⁹ Due to the large amount of recent publicity about raids and the establishment of new official and unofficial organizations to combat them, this calling scheme apparently works because it usually does not occur to the victim that the caller is just one more raider.⁶⁰ According to one expert, raiders have also recently begun to employ hackers to break into the computers of the target company and obtain confidential information for use in an upcoming raid.⁶¹

Having determined that the target is sufficiently attractive, the raider begins its attack, usually by putting in place one of the schemes described *supra*. Whatever the tactic, it is often accompanied by the filing of one or more civil suits against the target company. Even when civil litigation is not used as the basic scheme, it can be used as a supplementary tactic to obtain information about the target company (for example, through disclosure of documents by the target during court proceedings) or to harass the target and tie up its business in order to make it more willing to sell out to the raider at a below-market price. According to one analyst, in addition to ordinary civil litigation, raiders have also begun to use environmental activists to file suits for orders enjoining the operation of target factories on the grounds that they present an environmental hazard. If successful, such suits tie up the target's business and make it more vulnerable to a raid.⁶²

Another important supplementary tactic is the creation and presentation of false evidence in civil litigation. For example, in answering claims by victims, raiders typically offer false evidence, such as fabricated contracts and corporate resolutions, to "prove" the

56. *Id.*

57. ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 19-20; Novitskii, *supra* note 3, at 5.

58. Novitskii, *supra* note 3, at 8.

59. Inna Romanova, *Zakhvat po telefonu*, ROSSIYSKAYA GAZETA, Aug. 30, 2007, <http://www.rg.ru/2007/08/30/moschenniki.html>.

60. *Id.*

61. Novitskii, *supra* note 3, at 9.

62. IONTSEV, *supra* note 11, at 84.

alleged legitimacy of their acquisitions. One expert even concludes that presentation of false evidence in civil proceedings is a “required element” of raiding schemes.⁶³

In addition, raiders often exercise corrupt influence—through bribery, political pressure, or other means—over the judge(s) presiding over the case. According to statistics compiled by a non-governmental organization that tracks corruption, the National Anti-Corruption Committee (NACC), judicial decisions are easily bought and cost, on average, \$35,000.⁶⁴ Although explicit evidence of judicial corruption in raiding cases is rare, more evidence has recently come to light. In 2006, the Russian Supreme Court upheld the dismissal of a judge in Ingushetiya on the grounds that he had knowingly entered a corrupt and illegal decision that facilitated the raid of an oil extracting factory.⁶⁵ And in May 2008, Yelena Valyavina, a judge on Russia’s High Arbitrazh Court (the highest court empowered to hear corporate disputes) testified, in the context of a related libel suit, that a member of the Presidential Administration had threatened to block her reappointment to the bench if she did not rule as he demanded in a case involving an alleged raid on a major industrial concern.⁶⁶

In addition to civil litigation, raiders often use criminal cases to incapacitate targets and make them more vulnerable to raids. The use of so-called “commissioned criminal cases” (*zakaznye dela*) as a method of business sabotage has become so widespread that even Prosecutor General Yury Chayka acknowledged it and promised to take measures against it.⁶⁷ Commissioned cases can facilitate raids in several ways. These include obtaining information on the target company through the execution of search warrants at the company’s offices, as was allegedly done in the Hermitage Capital case.⁶⁸ In addition, the arrest and detention of the target’s principals incapacitates them and makes it much harder for them to resist a raid. For example, lawyers for reputed organized crime figure Semyon Mogilevich and his business partner, Alexander Nekrasov, claim that their clients’ 2008 arrests for tax violations allegedly committed through the company Arbat Prestizh are part of an attempt by a raider to incapacitate them and take over the company.⁶⁹

Another reportedly common tactic is the so-called “Black PR” campaign, consisting of dissemination of false information about the target through the mass media in order to lower its price per share and ripen it for a takeover.⁷⁰ This approach can also be used to facilitate the use of other tactics. For example, as one expert points out, because Russian

63. P.A. SKOBLIKOV, ARBITRAZHNYI I UGOLOVNYI PROTSESSY: KOLLIZII V SFERE DOKAZYVANIYA I PUTI IKH PREODOLENIYA 28 (Norma 2008).

64. Anastasiya Kornya, *Glavnyi reider—eto chinovnik*, VEDOMOSTI, Sept. 5, 2008, <http://www.vedomosti.ru/newspaper/article.shtml?2008/09/05/160078>.

65. Olga Pleshanova, *Sudya podnyela sebya pod sledstviye*, KOMMERSANT, July 22, 2008, http://www.ombudsman.gov.ru/dad_2008/dad07/dad853/06.doc.

66. Olga Pleshanova, *Sud vyshego dostoinstva*, KOMMERSANT, May 13, 2008, <http://www.kommersant.ru/doc.aspx?DocsID=891082>.

67. Yuri Chayka *prekratit “zakaznye dela”*, LENTA RU, Aug. 15, 2006, <http://lenta.ru/news/2006/08/15/chaika/>.

68. For example, in the Hermitage Capital case, the victims assert that raiders obtained internal corporate documents in an MVD search of the offices of Hermitage’s lawyers. Mortished, *supra* note 7.

69. See e.g., Alexander Dubrov, *Presumptsiya vinovnosti*, ROSSIYSKAYA GAZETA, Apr. 30, 2008, <http://www.rg.ru/2008/04/30/reidery.html>.

70. IONTSEV, *supra* note 11, at 84-85; Novitskii, *supra* note 3, at 8-9.

law permits the opening of a criminal investigation based on newspaper reports, such negative publicity schemes can also be used to start criminal cases.⁷¹

Actual and threatened force can also play an important role in raids. As was alleged in the Ilim Pulp case, many raids involve some combination of police, private security forces, court bailiffs, or simply hired thugs taking physical control of the target company, ostensibly to effectuate a court order or corporate resolution transferring the business and/or its assets.⁷² For example, in February 2004, raiders allegedly orchestrated the kidnapping of the son and daughter of the director of the Moscow Transportation Agency (*Mostransagentsvo*) and then demanded that he sell his shares to them.⁷³ In the Kumarin case, Barsukov has been charged with the attempted murder of the director of an oil terminal as part of an alleged raid on the victim's business.⁷⁴

Finally, as stated above, a raid is usually completed with the rapid transfer of the seized assets through a series of shell companies to an ostensible "good faith purchaser." An August 2008 Report by the NACC cites a typical case in which raiders falsified corporate documents and transferred the seized assets through a series of offshore shell companies to another offshore shell company. Relying on its alleged good faith purchaser status, the offshore shell company then sent in its security forces to forcibly remove the real owners from the property.⁷⁵ Similarly, Vladimir Ovchinskii, one of Russia's leading experts on organized crime and a former MVD investigator, cites the use of ostensible good faith purchasers as the main instrument through which raids are accomplished.⁷⁶ This technique is apparently so widespread that it has even been made into popular fiction about raiding. For example, in Pavel Astakhov's novel, *Raider*, a lawyer explains to the victim of a raid:

You can rest assured that, by early next week, they will affect the sale of the [business which has been raided] to their subsidiary firm. And then they'll sell it again to whomever commissioned the raid as a so-called good faith purchaser, from whom it will be almost impossible to take it back.⁷⁷

As will be discussed *infra*, Russian law makes it difficult to recover any property from a good faith purchaser; thus, once the seized property is safely in the hands of a party claiming to be a "good faith purchaser," the raid is practically irreversible.⁷⁸

71. Novitskii, *supra* note 3, at 12; Ovchinskii, *supra* note 27.

72. See, e.g., ASTAKHOV-REIDER, *supra* note 5, at 9-12 (providing a vivid, though fictional, account of such an armed takeover).

73. Vitaliy Kamyshev, *Biografiya Chayki izobiluyet koloritnymi epizodami na fone kotorykh bledneyut grekhi nezadachlivovo 'kbodoka' Skuratova*, KOMPROMAT RU, May 14, 2007, <http://www.compromat.ru/main/chaika/a.htm>; IONTSEV, *supra* note 11, at 38.

74. Delo, *supra* note 40.

75. PREDLOZHENIYA PO POVYSHENIYU EFFEKTIVNOSTI BORBY S REIDERSTVOM (NEZAKONYM ZAKHVATOM SOBSTVENNOSTI) (Aug. 15, 2008) (unpublished manuscript, on file with author) [hereinafter NACC Report].

76. Ovchinskii, *supra* note 27, at 20-21.

77. ASTAKHOV-REIDER, *supra* note 5, at 84.

78. See, e.g., IONTSEV, *supra* note 11, at 77; ASTAKHOV-REIDER, *supra* note 5, at 80.

B. CAUSES

Why is raiding so prevalent in contemporary Russia? At least four causes can be readily identified. First is the general uncertainty of property rights resulting from the privatization of state assets in the early 1990s. As discussed *supra*, because the legal basis for so much of the privatization of state assets after the collapse of the Soviet Union was so vague, almost any property is subject to a challenge that it was illegally acquired. This situation, in turn, creates the possibility for allegations of other improprieties regarding the business and its holdings. These all provide a basis for the lawsuits and criminal investigations that, as discussed *supra*, play such an important role in raiding schemes. In identifying the factors that make raiding possible, Vadim Volkov lists first "the defects and tensions created by earlier privatization policies."⁷⁹

A second cause of the prevalence of raiding is corruption in law enforcement and the judicial system. As discussed *supra*, raids often depend on commissioned criminal investigations and inspections of the target business and purchased judicial orders. A recent report by the NACC focused on corruption in law enforcement as a major cause of raiding, concluding that "state agencies play an extraordinarily important role in the realization [of raiding schemes]."⁸⁰ Pavel Astakhov came to the same conclusion, writing that "[c]orruption [and] the absence of a strong independent judiciary. . . have led to a situation in Russia in which it is cheaper to steal a business than to acquire it legitimately."⁸¹

A third cause is poor corporate governance. In 2000, one study ranked Russia last among twenty-five emerging countries regarding responsible corporate governance.⁸² In 2001, one leading political figure told the American Chamber of Commerce, "It's clear that despite nearly 10 years of economic changes, we have not yet developed a culture where people understand properly the relationship between managers, shareholders, minority shareholders and the state."⁸³ A 2003 World Bank report stated that "[p]oor corporate governance has been one of the main stumbling blocks in Russia's uneven transition to a market-based economy."⁸⁴ Thus, it is not surprising that, as discussed *supra*, many raiding schemes grow out of shareholder disputes and rely on illegal access to internal corporate records and manipulation of the target's company's stock and internal regulations. In a recent report, the NACC stressed the absence of adequate legal measures for protecting the rights of minority shareholders. According to the report, current Russian legislation does not provide sufficient defenses for minority shareholders in cases where, for example, majority shareholders render minority shares worthless through a corporate reorganization. In such cases, the NACC concluded, minority shareholders are left with no option but to employ the services of professional raiders to get their property back.⁸⁵

79. Volkov, *supra* note 17, at 546.

80. NACC Report, *supra* note 75, at 12.

81. ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 7.

82. Sheila M. Puffer & Daniel J. McCarthy, *The Emergence of Corporate Governance in Russia*, in CORPORATE GOVERNANCE IN RUSSIA 5 (Daniel J. McCarthy, Sheila M. Puffer, Stanislav V. Shekshnia eds., Edward Elgar Publishing 2004).

83. *Id.*

84. *Corporate Governance in Russia: Regime Change Required*, BEYOND TRANSITION: THE NEWSLETTER ABOUT REFORMING ECONOMIES (The World Bank Group, Washington, D.C.) Jan. 2003, www.worldbank.org/html/prddr/trans/janfebmar03/pg21.htm.

85. NACC Report, *supra* note 75, at 6-7.

A final, readily identifiable cause of raiding is the fact that the legal system is simply not yet equipped to deal with this novel form of crime. The gap between crime and the law is not a new problem. Examples from U.S. history include the period in the late 19th and early 20th centuries before the passage of anti-trust laws and, more recently, the periods before the passage of new criminal statutes addressing high tech crimes like hacking and spamming.

Each one of these causes deserves an article, if not more. The remainder of this article, however, will focus on the last cause—the legal gaps, particularly in the criminal law and the structure of the court system, that facilitate criminal raiding. This choice is partly dictated by the fact that inadequate legislation is the cause most easily remedied. For example, as discussed *supra*, the 2002 amendments to the bankruptcy law led to a reduction in bankruptcy raiding. Similarly, changes to the Japanese Commercial Code in 1982 significantly reduced the criminal practice of *sokaiya*, or corporate extortion.⁸⁶ Of course, law itself is not a panacea and must, as Volkov says, be evaluated in terms of the extra-legal reality in which it is applied.⁸⁷ But, it is still important in its own right as it creates incentives and disincentives for certain kinds of behavior. While amendments to the law in and of themselves may not be sufficient to eradicate the problem completely, such amendments can help to alleviate the problem and are therefore worthy of attention.

1. Court Structure

The biggest loophole facilitating raiding may be the very structure of the Russian court system. Russia has a tripartite court system consisting of (1) arbitrazh, or commercial, courts that have jurisdiction over disputes between legal entities and between the state and legal entities; (2) courts of general jurisdiction that are empowered to hear criminal cases, as well as civil disputes between individuals and legal entities; and (3) the Constitutional Court that is authorized to hear challenges to the constitutionality of certain statutes.⁸⁸ The split between criminal and commercial courts creates a “ping pong” effect in raiding cases in which victims are told by arbitrazh courts that their conflict is essentially criminal and should be heard in a court of general jurisdiction. When the victims approach law enforcement seeking initiation of a criminal case, however, they are told that the conflict is essentially a business dispute that should be resolved through civil litigation. In the end, the victims wind up in a legal netherworld from which there is no escape.⁸⁹ For example, one analyst, Pyotr Skoblikov, cites a case in Krasnodar in which a bank filed suit in arbitrazh court against a loan recipient who had allegedly fraudulently obtained credit from the bank and failed to repay the debt. At the same time, the bank sought a criminal prosecution of the debtor. After the arbitrazh court ruled the bank’s petition meritorious, the criminal investigator closed the criminal investigation on the grounds that, in light of the arbitrazh court’s ruling, the dispute was clearly a commercial one that should be resolved through civil litigation rather than criminal prosecution.⁹⁰ Thus, ironically, the

86. See SZYMOWIAK, *supra* note 1, at 18 (reporting that the number of *sokaiya* dropped from 6,783 in 1982 to 1,682 in 1983 as a result of the reform).

87. Volkov, *supra* note 17, at 545.

88. WILLIAM BURNHAM, PETER B. MAGGS & GENNADY M. DANILENKO, LAW AND LEGAL SYSTEM OF THE RUSSIAN FEDERATION 50 (Juris Publ’g, Inc. 3d ed. 2004).

89. SKOBLIKOV, *supra* note 63, at 80.

90. *Id.* at 14.

very fact that the bank's civil suit was deemed meritorious provided the grounds for closing the parallel criminal investigation.

According to Skoblikov, as in the Krasnodar case, investigators often terminate or suspend criminal investigations as soon as they learn that there is a related pending civil case.⁹¹ This lull provides an opportunity for a raider who is the subject of a criminal investigation to concoct a civil suit that has some relationship to the criminal investigation (it does not even matter if the raider is plaintiff or defendant in the civil case) and then petition for the suspension of the criminal case on the grounds that there is a related pending civil case. There is also the possibility of the inverse scheme, i.e., defeating a threatened or actual civil suit by commissioning a criminal case against oneself. Russian criminal cases still use a bound case file or dossier (*delo*) that contains all the evidence compiled by the investigator during the period of preliminary investigation.⁹² The *delo* is maintained by the court and documents cannot be removed from it; hence, it is impossible for an arbitrazh court to obtain potentially necessary evidence if the case being litigated is the subject of a related criminal proceeding.⁹³

There are other ways in which the split between the commercial and criminal courts can be exploited by raiders. As we have seen, presentation of false evidence in arbitrazh courts is a central feature of many raiding cases. Under Article 161 of the Arbitrazh Procedure Code, a party against whom a false document has been offered can make a formal challenge to the document on the grounds of its alleged falsity (*zayavleniye o falsifikatsii*).⁹⁴ The arbitrazh court, however, lacking authority to hear criminal matters, has only limited power to determine whether the document is, in fact, false.⁹⁵ If the party against whom the accusation is made agrees to the removal of the offending document from the case file, the inquiry ends, thus placing him in a no-lose situation.⁹⁶ An arbitrazh court that investigates the claim could be accused of overstepping its authority and has no choice but to refer the matter to law enforcement.⁹⁷ The law provides no mechanism, however, for an arbitrazh court to make such a referral, and the highly formalized Russian system does not recognize informal referrals.⁹⁸ If the offended litigant himself goes to law enforcement, he may well be turned away, as in the Krasnodar case, on the grounds that his dispute is essentially civil. Even if he succeeds in starting a criminal case against the party offering the false document, prosecuting such a case could take years. By the time the criminal case is concluded, irreparable damage will likely have been done. Clearly, combating raiding requires the development of mechanisms for exchange of evidence between arbitrazh courts and courts of general jurisdiction and for coordinating related civil and criminal litigation.⁹⁹

91. *Id.* at 24.

92. William Burnham & Thomas Firestone, Investigation of Criminal Cases under the Russian Criminal Procedure Code, 3 (Oct. 29, 2007) (unpublished manuscript, on file with author).

93. SKOBLIKOV, *supra* note 63, at 25-26.

94. Arbitrazhno-Protessualnyi Kodeks [APK] [Code of Arbitration Procedure] art. 161 (Russ.).

95. SKOBLIKOV, *supra* note 63, at 57.

96. Arbitrazhno-Protessualnyi Kodeks [APK] [Code of Arbitration Procedure] art. 161(1)(3) (Russ.).

97. SKOBLIKOV, *supra* note 63, at 57.

98. *Id.* at 59.

99. Moreover, the split between commercial and civil courts means that criminal judges are often ill-prepared to deal with the complicated commercial issues that may arise in criminal raiding prosecutions. Con-

2. *Inadequacy of the Criminal Law*

The loopholes created by the structure of the court system only make it more imperative that law enforcement combat raiding through criminal prosecutions. The criminal law, however, also contains several shortcomings that make this task difficult. Primary among these loopholes is the absence of an article in the Criminal Code specifically criminalizing raiding. While the Criminal Code contains articles on fraud (Article 159); extortion (Article 163); bankruptcy fraud (Articles 196 and 197); securities fraud (Articles 185 and 186); illegal collection of commercial information (Article 183); commercial bribery (204); and organization of a criminal society (Article 210), there is no article specifically addressing raiding. In the few cases that are brought, raiding is generally charged as fraud under Article 159. This article is a poor substitute for one directly on point.

For example, the elements of raiding often do not correspond exactly to the elements of fraud, defined in Article 159 as "the stealing of another's property or the acquisition of the right to another's property by means of deceit or abuse of trust."¹⁰⁰ Imagine, for example, a case in which a raider files a lawsuit against the target company and then blackmails the judge into entering an order authorizing the raider to seize the target company. There is no deceit or abuse of trust, so the raider could not be charged with "fraud." Nor could he be charged with extortion, defined as:

demanding the transfer of another's property or the right to property or the commission of other actions of a property character under threat of the application of force or the destruction or damaging of another's property, and likewise under threat of the dissemination of information defaming the victim or his relatives, or other information which may cause material harm to the rights or legal interests of the victim or his relatives.¹⁰¹

There has, after all, been no direct threat of defamation to the victim (as opposed to the judge).

Russia's organized crime statute, Article 210 of the Criminal Code, also appears inadequate to capture raiding cases, as it requires proof that the criminal group committed serious or especially serious crimes (defined respectively, under Russian law, as crimes punishable by six to ten years incarceration and ten-plus years incarceration).¹⁰² Many of the crimes at the heart of raiding, however, such as presentation of false documents in civil litigation, carry much lighter penalties and do not qualify. In addition, many existing statutes used to prosecute raiding do not carry penalties commensurate with the crime. For example, even in its most aggravated form, fraud is punishable by a maximum of ten years incarceration.¹⁰³ Extortion that does not involve force, as in the hypothetical above, is punishable by a maximum of three years incarceration.¹⁰⁴ In short, raiding does not fit

versely, commercial court judges are unlikely to be familiar with the criminal issues that may arise in civil litigation related to raiding.

100. Art. 159, Criminal Code. (The translation of the Criminal Code used in this article is CRIMINAL CODE OF THE RUSSIAN FEDERATION (William E. Butler trans. Simmonds & Hill Publ'g Ltd. 3d ed. 1999)).

101. Art. 163, Criminal Code.

102. Ugolovnyi Kodeks [UK] [Criminal Code] art. 210 (Russ.).

103. Ugolovnyi Kodeks [UK] [Criminal Code] art. 159(4) (Russ.).

104. Ugolovnyi Kodeks [UK] [Criminal Code] art. 163 (1), (Russ.).

comfortably within the elements of existing crimes and therefore requires a new criminal statute.¹⁰⁵

A number of proposals have been offered to fill this gap. For example, the NACC proposes adding an article to the criminal code, which would read as follows:

Raiding, that is, acts designed to give a legitimate appearance to the illegal (accomplished through illegal means) transfer to the actor or a third party, property rights, rights to the results of intellectual activity and equal rights to individualization (of intellectual rights) as well as, the illegal acquisition of the right to carry out managerial functions in a commercial or other organization is punishable by . . . up to six years incarceration.¹⁰⁶

A draft law introduced in the Duma by the Duma's Security Committee in March 2008 proposes to make raiding an aggravating circumstance of other crimes and provides a broader definition than that contained in the NACC proposal. Specifically, it defines raiding as the "commission of a crime connected with the illegal acquisition of the right of ownership, and/or use, and/or management of the shares of participants in a legal entity in the charter capital of a legal entity and/or voting shares of a stock company."¹⁰⁷

Upon scrutiny, both of these proposals appear inadequate. While the NACC proposal captures the aspect of raiding that relates to the transfer of assets through shell companies to a good faith purchaser, it fails to capture the initial illegal acquisition of the assets—the key aspect of any raid. Moreover, insofar as it addresses the initial acquisition, it criminalizes only the acquisition of the "right to carry out managerial functions in an organization" but not the acquisition of the target company's assets. Thus, the NACC proposal seems to provide an enormous loophole that would allow raiders to evade prosecution by simply arranging for a front man to serve as manager of the stolen enterprise. Finally, the proposed penalties are relatively weak. Under the draft law, if a prosecutor is unable to prove that the raid was carried out with official participation—an element that may well be difficult to prove—the maximum sentence will be limited to six years, substantially less than the ten-year penalty available in cases of fraud carried out by an organized group.¹⁰⁸ Therefore, prosecutors will likely continue to use the fraud statute, with all of its weaknesses, thus defeating the purpose of the new legislation. While the Security Committee proposal is appropriately focused on the illegal acquisition of the corporation itself, it fails to define exactly what makes such acquisition illegal and would therefore also likely be unusable in practice.

Although the United States does not have a raiding statute per se, RICO criminalizes acquiring control of an enterprise through a pattern of racketeering activity, defined as the commission of two or more specified "predicate acts" within a ten-year period.¹⁰⁹ Russia

105. In an interview with the author, Sergei Golkin, an experienced raiding investigator with the Investigative Committee of the General Procuracy, agreed that a specific raiding statute would help law enforcement combat raiding.

106. NACC Report, *supra* note 75, at 21-22.

107. Yulia Vasil'yeva, *Reid na 20 let: MVD predlagayet usilit' nakazaniye za nezakonnyi zakhvat sobstvennosti*, ROSSIYSKAYA BUSINESS-GAZETA, Sept. 2, 2008, <http://www.rg.ru/2008/09/02/reidery-nakazanie.html>.

108. The proposed law provides for enhanced penalties for raiding carried out with the assistance of government officials (5-8 years' incarceration) and for raiding carried out by government officials (8-12 years' incarceration). NACC Report, *supra* note 75, at 22.

109. 18 U.S.C. § 1961(5) (2007).

might do well to consider adopting a similar statute criminalizing the takeover of a business through the commission of one or more predicate crimes, a list that could include, *inter alia*: fraud, blackmail, extortion, falsification of corporate documents, presentation of false evidence in civil litigation, bad faith filing of frivolous lawsuits, bad faith instigation of criminal investigations, commercial bribery, and intentional dissemination of false information through the mass media. To be effective, the statute must carry severe penalties. Such a statute would provide a definition that encompasses the full range of criminal activity associated with raiding, while remaining workable and flexible by allowing prosecutors to appropriately tailor charges to fit the facts of a particular case.¹¹⁰

Another aspect of Russian criminal law that likely contributes to raiding is the weakness of penalties for presentation of false evidence in civil litigation. For example, Article 303 of the Criminal Code, which prohibits falsification of evidence in civil proceedings, provides for a maximum penalty of only four months incarceration.¹¹¹ Similarly, giving of false testimony is punishable by a maximum of only three months incarceration.¹¹² By contrast, U.S. law provides for a maximum penalty of twenty years incarceration for falsification of evidence and a maximum of five years incarceration for perjury.¹¹³ As one expert has written, the punishments for these crimes are largely symbolic and even the short sentences provided for in the law are rarely imposed.¹¹⁴ In addition, as discussed *supra*, a party can avoid liability altogether by simply withdrawing the proffer of the documents.¹¹⁵ Frequent litigants in Russian arbitrazh courts told the author that obstruction of justice in civil cases in Russia is extremely common because the penalties are so low and so rarely enforced.

Thus, it is not surprising that raiding schemes frequently rely on the falsification of documents, such as shareholder registers and contracts, and the presentation of these falsified documents in arbitrazh court proceedings. The Duma Security Committee's proposed legislation would heighten penalties to a range of two to five years for falsification committed as part of a raid.¹¹⁶ This change is clearly appropriate, but it is not clear why the proposed enhancements would be limited to falsification in connection with a raid, an added element that essentially requires prosecutors to prove the raid before they can prove the falsification, which could make it difficult to use these provisions effectively.

Another serious loophole in Russian criminal law impeding the investigation and prosecution of raiding is the absence of corporate criminal liability. Article 19 of the Russian Criminal Code limits application of the criminal law to "natural persons," thus excluding

110. The introductory part of the NACC Report proposes something similar, defining raiding as "the distribution of property accomplished through acts which are punishable criminally or administratively" and provides as examples of such acts "blackmail, coerced transactions, falsification of documents, exceeding official authorization and so on." For some reason, though, this definition is not used in the Committee's proposed legislation. NACC Report, *supra* note 75, at 6.

111. Ugolovnyi Kodeks [UK] [Criminal Code] art. 303(1) (Russ.).

112. Ugolovnyi Kodeks [UK] [Criminal Code] art. 307(1) (Russ.).

113. 18 U.S.C. § 1512(C)(1) (2008) (covering alteration of records, documents, or other objects with the goal of impairing their integrity or availability for use in an official proceeding); 18 U.S.C. § 1621 (2008) (covering perjury).

114. SKOBLIKOV, *supra* note 63, at 79.

115. *Id.* at 53; interview with Victoria Shaking, attorney, in Moscow, Russ. (July 2008).

116. *V Dum vnesyon proekt, uzbekostchayuschii orvetsvoennost' za reiderskiye Zakbvatii*, BUGHALTERIA RU, Mar. 24, 2008, <http://www.buhgalteria.ru/news/17179>.

the possibility of corporate prosecutions.¹¹⁷ Raids, however, are almost always accomplished through corporate structures. As one expert on raiding states, "The greatest danger is presented by raider-companies—firms, which have made taking over enterprises their business."¹¹⁸ Another analyst concluded, based on a survey of businesses, that large companies are the main initiators of raids.¹¹⁹ The NACC Report also notes that large financial-industrial groups and small and medium companies are among the leading raiders in contemporary Russia.¹²⁰ These assessments are consistent with the allegations in many of the most notorious raiding cases. For example, the Base Metals raids were allegedly carried out by a number of corporate entities named as defendants in the U.S. lawsuits, including Russian Aluminum, Rual Trade Ltd., Sibirsky Aluminum Products, Bauxal Management, Metcare Management, and many others.¹²¹ Boyko is alleged to have carried out the illegal takeover of suburban Moscow property through the company "Your Financial Adviser."¹²² According to another expert, Ovchinskii, one of the most dangerous raiding organizations is a corporate entity called RBE, which managed to corruptly acquire several properties belonging to the Ministry of Defense.¹²³

Absent a mechanism for prosecuting the corporation itself, as opposed to prosecuting just certain individuals within the corporation, raiding corporations will be able to continue to operate through front men, while escaping liability themselves. None of the draft anti-raiding legislation currently under consideration, however, including the NACC proposals, the Duma Security Committee's proposed amendments, and draft legislation submitted by the Duma Property Committee, would introduce corporate criminal liability.¹²⁴

3. *Criminal Investigation*

In addition to these gaps in Russia's substantive criminal law, there are also aspects of the law governing criminal investigation and procedure that inhibit the effective investigation of complex crimes such as raiding. Primary among these is the absence of legislation providing mechanisms for obtaining and using testimony from cooperating witnesses. Almost every successful federal organized crime and/or white collar crime prosecution in the United States relies on the testimony of at least one cooperating witness. As Judge Stephen S. Trott has written:

117. Ugolovnyi Kodeks [UK] [Criminal Code] art. 19 (Russ.).

118. Novitskii, *supra* note 3, at 3.

119. Igor Bunin, *Reiderstvo kak sotsial'no-ekonomicheskii i politicheskii fenomen sovremennoi Rossii* 25 (May 2008) (unpublished manuscript, on file with author).

120. NACC Report, *supra* note 75, at 11.

121. *Base Metal Trading Ltd. v. Russian Aluminum*, 98 F. App'x 47, 47 (2d. Cir. 2004).

122. Vladislav Trifonov, *Vasiliiu Boiko nasbli prestupnyy grupp i gendirektora i glavnogo yurista ego kompanii*, KOMMERSANT, June 5, 2007, <http://www.kommersant.ru/doc.aspx?DocsID=771674>.

123. Ovchinskii, *supra* note 27, at 19.

124. At a conference at Moscow State University Criminal Law Faculty on May 30, 2008, attended by the author, many Russian criminal law scholars reacted hostilely to the concept of corporate criminal liability, arguing that a corporation cannot form "criminal intent" and that Russia's court structure, which requires cases involving corporations to be heard in commercial courts rather than courts of general jurisdiction (which are the only courts authorized to hear criminal cases), cannot implement corporate criminal liability. These sentiments were echoed by a Duma deputy, who told the author that Russia is simply not ready for corporate criminal liability. Meanwhile, another government official, whose responsibilities include drafting new criminal legislation, told the author that corporate criminal liability will never pass the Duma because too many Duma deputies launder their illegal proceeds through corporate vehicles.

Notwithstanding all the problems that accompany using criminals as witnesses, the fact of the matter is that police and prosecutors cannot do without them-period If a policy were adopted never to deal with criminals as prosecution witnesses, many important prosecutions-especially in the area of organized and conspiratorial crimes-could never make it to court.¹²⁵

Cooperating witnesses could provide essential testimony in raiding cases establishing, for example, criminal intent on the part of the raiders, the falsity of documents presented in support of the scheme, or the fact that alleged good faith purchasers are in fact co-conspirators to the scheme. In contrast to U.S. law, however, which explicitly recognizes the value of accomplice testimony and offers statutory incentives (including the possibility of a major sentence reduction) for the provision of such testimony,¹²⁶ Russian law provides no effective means for obtaining the testimony of cooperating witnesses.¹²⁷ Russian investigators, prosecutors, and defense attorneys have repeatedly told the author that defendants are unwilling to cooperate due to the absence of legally sanctioned rewards for cooperation. The absence of such a mechanism is especially detrimental in raiding cases given the complicated nature of the schemes and the frequent absence of direct evidence against all of the co-conspirators. For example, a journalist who has covered the Kumarin case told the author that Kumarin was careful to keep his name off almost all of the relevant documents and that the case against him will be difficult to prove without an insider who can provide direct testimony of his involvement. In a conversation with the author, the lead investigator on the Kumarin case agreed that cooperating witness legislation would help in the investigation of raiding.

Although none of the proposed anti-raiding legislation addresses cooperating witnesses, in early 2008, the Duma's Security Committee introduced a draft law that would cap sentences at one half of the statutory maximum and empower judges to disregard any statutory minimum sentence upon a finding (supported by a prosecutor's certification) that the defendant had provided substantial and truthful cooperation in the investigation and prosecution of other crimes.¹²⁸ The draft law encountered opposition in the Duma, however, on the grounds that it would allow criminals to escape punishment and might stimulate corruption within law enforcement.¹²⁹ It is not clear when, or if, the draft law will pass.

Closely connected to the issue of cooperating witness testimony is witness protection. Given the frequency with which violence is used in raids, witnesses in such cases could be in great danger and would likely be unwilling to testify without assurance of their safety.

125. Hon. Stephen S. Trott, *Words of Warning for Prosecutors Using Criminals as Witnesses*, 47 HASTINGS L.J. 1381, 1390-91 (July/August 1996).

126. See, e.g., UNITED STATES SENTENCING GUIDELINES MANUAL § 5K1.1, (stating that defendants who provide "substantial assistance" to law enforcement may be sentenced below the otherwise applicable sentencing range).

127. For a more thorough discussion of this subject, see Thomas Firestone, *What Russia Must Do to Fight Organized Crime*, 14 DEMOKRATIZATSIYA 59 (2006).

128. See Federal'nyi Zakon "O Vnesenii izmenenii v Ugolovnyi kodeks Rossiiskoi Federatsii i Ugolovno-protessual'nyi kodeks Rossiiskoi Federatsii" (o vvedenii osobogo por'yadka vyneseniya sudebnogo soglasheniya o sotrudnichestve).

129. See Elya Vermisheva, *Gosduma posbla na sdyelki s pravosudiyem*, GAZETA RU, Feb. 15, 2008, www.gazeta.ru/social/2008/02/15/2638051.shtml; N. A. Lopashenko, *Zaklyucheniye na proyekt Federal'nogo Zakona*, No. 4, (2007) (unpublished manuscript, on file with author).

In January 2005, Russia's first witness protection legislation, titled "A Federal Law on Government Protection of Victims, Witnesses, and Other Participants," took effect. Although it provides for a variety of protective measures for victims and witnesses—including "protection of home and property," "individual protection, communication, and security alarm devices," "relocation," "issuance of new documents," "change of appearance," "transfer to a new job or educational institution," and "temporary relocation to a secured shelter"—critics claim that its implementation has been marred by lack of sufficient funding,¹³⁰ the population's distrust of law enforcement, and suspicion that corrupt officials charged with their protection will, for a price, turn them over to the very people who present a threat.

4. *"The Good Faith Purchaser"*

In addition to these problems with the criminal justice system, the civil law's failure to provide adequate mechanisms for defeating fraudulent claims by alleged "good faith purchasers" presents another obstacle to combating raiding. As discussed *supra*, most raiding schemes rely on the rapid transfer of the victim's assets to an ostensible "good faith purchaser." The claim of a good faith purchaser can be defeated by proof sufficient to sustain his criminal conviction as a co-conspirator. Doing this is almost impossible, however, absent an anti-raiding statute and a system of cooperating witnesses. Moreover, also as discussed *supra*, the structure of the court system means that criminal raiding cases may wind up in the exclusive jurisdiction of a civil court. Therefore, combating raiding requires that the civil law provide a remedy that can be applied short of a criminal conviction.

Article 167 of the Russian Civil Code provides that when a transaction is declared invalid, each of the parties to the transaction must return to the other everything each has received in the deal or make appropriate monetary compensation.¹³¹ In a ruling dated April 21, 2003, however, Russia's Constitutional Court¹³² held that these provisions "cannot be extended to a good faith purchaser unless this is specifically provided by statute."¹³³ What this ruling means, as a practical matter, is that even if a raiding victim succeeds in obtaining a court ruling voiding the transfer of his company's assets, he cannot recover those assets from a third party good faith purchaser. For example, in the case of Kenotek, the plaintiffs, shareholders of the company Kenotek, claimed that certain members of the board of directors had sold real property to a company in which they had an interest—Meret-K—at the expense of Kenotek's shareholders. Meret-K then sold the property to a company called Sib Monolith, which, in turn, sold it to a company called Meret. The Federal Arbitrazh Court of the West Siberia federal district held that, regardless of the merits of the plaintiffs' claims (and regardless of the obvious relationship between Meret

130. Mikhail Dobrovolski, *Svidetel' pod zashitoi*, Apr. 27, 2007, http://www.aferizm.ru/criminal/k_svidetel_zaschita.htm; Valeriya Podorozhnova, *Dopros pod pseudonimom: pochemu ne rabotayet zakon o zashite svidetelyei*, Dec. 18, 2007, <http://www.rg.ru/2007/12/18/reg-jugrossii/zaschitasvidetelya.html>.

131. *Grazhdanskii Kodeks [GK] [Civil Code]* art. 167 (Russ.).

132. The Constitutional Court was established in 1991 and, pursuant to the 1994 Law on the Constitutional Court, has the power to review the constitutionality of laws and other normative acts and to settle other commercial disputes. BURNHAM, *supra*, note 88, at 62, 64.

133. The Constitutional Court: Case Concerning Article 167 of the Civil Code, Ruling No. 6-P, VKS 2003, No.3 (Apr. 21, 2003), reprinted in BURNHAM, *supra* note 88, 353-56.

and Meret-K), the property could not be recovered from Meret in light of the Constitutional Court's April 21, 2003, decision.¹³⁴ As one commentator wrote, cases like Kenotek demonstrate the extent to which Russian civil law has failed to keep pace with the development of commercial relations.¹³⁵

The difficulties of recovering property from an ostensible good faith purchaser are further aggravated by a resolution of the High Arbitrazh Court dated October 11, 2005, holding both that a suit to nullify a transaction cannot proceed if one of the parties to the transaction has been liquidated and that the obligations of the liquidated entity cannot pass to a third party.¹³⁶ Therefore, if assets have been transferred through a front company that has subsequently been liquidated, the victim/plaintiff is essentially left without remedy. Taken together, these rules explain the widespread practice of transferring stolen assets through front companies to a good faith purchaser and then liquidating the intermediate company or companies.

By contrast, U.S. law allows for recovery of assets from a third party in a civil proceeding upon a showing that the purchaser "possesses knowledge of facts that suggest a transfer may be fraudulent."¹³⁷ In addition, some U.S. states recognize a "larceny exception" that defeats even a good faith purchaser's claim when it can be shown that the seller acquired title to the transferred property by larceny.¹³⁸ Given that the Constitutional Court's ruling specifically provided that Article 167 could be applied to good faith purchasers if provided for by statute, the Duma could enact legislation allowing for recovery of raided assets from good faith purchasers in civil cases upon a sufficient showing that the good faith purchaser knew or should have known that the assets he purchased were acquired illegally.¹³⁹

5. *Verification of Corporate Documents*

Another major oversight appears to be the absence of a provision in the Russian laws on corporate registration requiring registering authorities to verify the accuracy of the information presented to them.¹⁴⁰ As we have seen, raiding often involves the altering of internal corporate documents to reflect false changes in the board of directors. As Pavel

134. Resolutions of the Federal Arbitrazh Court of the West Siberia District (Postanovleniya FAS ZCO), Oct. 19, 2005, Nos. F04-5367/2005(1584-A27-5); F04-5367/2005(15252-A27-5), reprinted in V.N. TROFIMOV, *NEDEISTVITELNOST'* SDYELOK: SBORNIK SUDEBNOI PRAKTIKI S KOMMENTARIYAMI, 63-69 (2008).

135. TROFIMOV, *supra* note 134, at 69.

136. Resolution of the Presidium of the High Arbitrazh Court of the Russian Federation (Postanovleniye Presidiuma VAS RF), Oct. 11, 2005, No. 7278/05, reprinted in TROFIMOV, *supra* note, 134, at 40-42.

137. See, e.g., *Banner v. Kassow*, 104 F.3d 352, 352 (2d Cir. 1996).

138. *Dimension Funding LLC v. DKA Assocs., Inc.*, 191 P.3d 923, 926 (Wash.Ct. App., 2008).

139. In November 2008, the Supreme Arbitrazh Court issued Information Letter No. 126 entitled "Survey of Judicial Practice on Certain Questions Connected with Recovery of Property from Another Person's Unlawful Possession," which is available at <http://www.garant.ru/prime/20081216/1689369/htm>. Such information letters provide binding guidance to lower courts. Some of the language in Information Letter No. 126 suggests that courts should apply a restrictive definition of "good faith purchaser," which would exclude acquirers who knew or should have known that the transferor did not have the legal right to transfer the property in question. It is still too early, however, to say how Information Letter No. 126 will be interpreted and applied by lower courts, and legislation clarifying this point would provide a firmer basis for courts to invalidate fraudulent transfers to ostensible good faith purchasers.

140. ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 46.

Astakhov argues, this practice is partly facilitated by the absence of any requirement in the "Law on State Registration of Legal Entities and Individual Businessmen" that registering officials verify the information presented to them.¹⁴¹ Rather, the law simply requires that amendments to incorporation documents be entered within five days of their submission and does not identify the presentation of false documents as a ground for refusal to enter the amendments.¹⁴² Requiring state authorities charged with registering corporate changes to verify the authenticity of all documents presented to them before accepting them and imposing criminal liability for the presentation of false documents to registering authorities would undoubtedly make it more difficult for raiders to steal companies through manipulation of internal corporate documents.¹⁴³

III. Possible Remedial Measures

Clearly, raiding will continue as long as there is corruption in the court system and law enforcement. But, in the meantime, there are steps that could be taken to alleviate the problem. Specifically, Russia could:

- (1) create mechanisms allowing for the rapid exchange of evidence between arbitrazh courts and courts of general jurisdiction in related cases;
- (2) pass legislation specifically criminalizing raiding and establishing specialized task forces to investigate and prosecute raiding cases;
- (3) strengthen criminal penalties for the presentation of false evidence in civil cases and create a mechanism allowing arbitrazh courts to refer cases of suspected falsification to law enforcement for rapid adjudication;
- (4) amend the criminal code to allow for criminal prosecution of legal entities;
- (5) create legal mechanisms for obtaining and using cooperating witness testimony in court;
- (6) pass legislation allowing for the recovery, in civil litigation, of assets from good faith purchasers who had reason to know that the assets they purchased were fraudulently acquired by the seller; and
- (7) require registering officials to check and authenticate documents presented to the State Unified Register of Legal Entities that purport to reflect changes in corporate structure.

There are also certain measures that businesses can take to protect themselves. These measures include retaining qualified legal counsel to draft and review all incorporation documents and contracts, retaining corporate investigation firms to investigate partners

141. Federal Law No. 129-FZ, Aug. 8, 2001, on the State Registration of Legal Entities and Individual Businessmen, *available at* <http://www.legislationline.org/legislation.php?tid=2&lid=642>; ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 149.

142. Federal Law No. 129-FZ, Arts. 19 (on amending constituent documents), 23 (refusal to grant state registration), 25 (liability for illegal actions); ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2, at 46.

143. There are, undoubtedly, numerous other gaps in the law that facilitate raiding. For example, Astakhov points to the absence of concepts of fiduciary duty, the absence of mechanisms for bringing shareholder class action suits, the impossibility of establishing corporate takeover defenses such as staggered boards of directors, and super-majority voting requirements. ASTAKHOV-PROTIVODEISTVIYE, *supra* note 2. These appear to relate more to non-criminal takeovers and insider malfeasance, however, than to criminal raiding and are beyond the scope of this article, which is focused exclusively on criminal raiding.

and major customers, and, above all, always complying with all relevant laws and regulations. Failure to do the latter will only provide attackers with an opportunity to initiate the kinds of inspections and criminal investigations that are so often the springboard for successful raids.

