



Russian corruption:
**Domestic and
international
consequences**

**How—and why—the U.K. should
bolster anti-corruption efforts in
the Russian Federation**

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Foreword by Dominic Raab MP

This report provides a timely reminder of the unique challenges facing Russia, a country burdened with endemic corruption at a critical stage of its economic and political development. It contains stark analysis regarding both the nature and the scale of this criminality – illustrated by the estimated \$211.5 billion of illicit capital that left Russia between 1994 and 2011.

As the author explains, these crimes are not solely economic in dimension. There are victims who pay a higher price, such as Sergei Magnitsky, the whistle-blowing lawyer who exposed a massive fraud perpetrated by a combination of state officials and organised crime. Through the connivance of those same officials and others, he was falsely arrested and then tortured in prison, where he eventually died after a year in detention.

This corruption is not a tragedy for the Russian people alone. The rest of the world suffers from its spill-over effects, through the drug trade, human trafficking, fraud and organised crime. Corruption in Russia inflicts damage and suffering on the streets of Britain.

It is unacceptable that the perpetrators are free to come to Britain, buy property and treat this country as a haven. As the report points out, Russian millionaires accounted for a quarter of the Tier-1 UK visas issued last year. Whilst most of these individuals will have earned their money legitimately, this report makes a powerful case for greater UK transparency (over who is coming to this country) and more robust law enforcement. It also strengthens the case for the enactment of a Sergei Magnitsky Act equivalent to the law passed in the United States in 2012, which would impose mandatory visa bans and asset freezes on those responsible for human rights abuses and cover-ups, wherever they are perpetrated.

Russia is a difficult partner, posing opportunities and presenting risks. We need to persevere in pursuing bilateral cooperation on issues from security to energy. However, in doing so we should not turn a blind eye to the tainting effect of corruption and other mafia criminality. If we do, these problems – and their international consequences – will only grow.



Dominic Raab
MP for Esher and Walton

March 2013

About the Russia Studies Centre

The Russia Studies Centre is a research and advocacy unit operating within the Henry Jackson Society. It is dedicated to analysing contemporary Russian political developments and promoting human rights and political liberty in the Russian Federation.

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EXECUTIVE SUMMARY

- **The Russian Federation has made tremendous strides since the economic chaos of the post-Soviet 1990s. However, the country remains plagued by endemic corruption, suffusing a system in which the boundaries between the public and private sector are blurred.**
- **This phenomenon has also gone hand-in-hand with the erosion of democratic development and return of authoritarianism under Vladimir Putin. It is used as a means of cementing the loyalty of the political elite, and flourishes in the absence of judicial independence and government transparency.**
- **According to polls, corruption is one of the foremost causes of dissatisfaction amongst the Russian public, and was one of the issues which inspired the mass protests of 2011-2012. Anti-corruption activism by individuals such as Alexey Navalny has highlighted the potential for this issue to be used as an impetus for political reform.**
- **While the Russian government has integrated international anti-corruption standards into its domestic legislation, those measures are selectively enforced, usually against political opponents. The government's most recent anti-corruption measures are unlikely to prove successful, as they do not address the need for systemic reforms such as the introduction of political competition, judicial independence and breaking the government monopoly on the media.**
- **Corruption in Russia is often tied, both directly and indirectly, to human rights abuses, by entrenching disrespect for individual**

rights in the political system. The case of the billionaire political prisoner, Mikhail Khodorkovsky, and the wrongful imprisonment and death of the whistleblower attorney Sergei Magnitsky aptly demonstrate this connection.

- Russian corruption undermines the economic prospects, civil liberties and fundamental dignity of the Russian population. However, the scale of this domestic problem also has significant ramifications in a globalised economy, as funds obtained through corruption are laundered and circulated throughout the world—often finding homes in global financial-centres such as London. Corrupt business practices exported into the international market undermine the stability and integrity of the international financial system.
- The United Kingdom has one of the most sophisticated anti-corruption regulatory structures in the world, and is internationally respected for its judicial independence. However, the enforcement of these regulations, particularly by banks and by agencies charged with oversight of the importation of funds tied to corruption, has consistently been criticised as insufficient by the Financial Services Authority (F.S.A.) and other bodies.
- The significant presence of Russian wealth and immigrants in the U.K. is a positive development. However, the likelihood of corrupt practices having been responsible for some Russian wealth should inform the assessment of funds brought into the country from Russia, as well as from other countries with reputations for corruption.
- Improved domestic enforcement is crucial to any effort by the U.K. to bolster anti-corruption efforts abroad. Banks should be subjected to increased pressure to engage in more rigorous assessments of risk in relation to funds from Russia and other corrupt countries. Additionally, investment in the Serious Fraud Office should be increased.
- The U.K. Parliament should undertake measures to enhance public scrutiny of corruption, including pushing forward libel reform. The current libel law regime aids those whose wealth is obtained through corruption by providing them with a significant

weapon with which to forestall investigations and silence public criticism of their activities.

- **Parliament should pass a U.K. version of the Sergei Magnitsky Rule of Law Accountability Act, which was signed into law in the United States in December 2012, and imposes visa bans and asset freezes on the individuals implicated in the imprisonment and death of Magnitsky, as well as any other Russian citizen credibly suspected of human rights abuses. If the U.K. passed a similar measure, this would have direct consequences for the individuals who engage in rights abuses, often for personal benefit via corrupt practices, and chip away at the incentives for participating in this system.**
- **The British government should increase its engagement with representative of Russia's embattled, but burgeoning, civil society. This should extend to high-level meetings with ministers in the Foreign and Commonwealth Office (F.C.O.), as well as engagement with parliamentary forums such as relevant All-Party Parliamentary Groups (A.P.P.G.s).**
- **The U.K. should robustly promote an anti-corruption agenda in international forums. In particular, the U.K. should use its G8 presidency this year to push for measurable benchmarks for Russia to undertake economic and political reforms relevant to a genuine systemic anti-corruption campaign.**

INTRODUCTION

In the past decade, the Russian Federation has emerged as one of the world's most promising economies, rising from post-Soviet economic chaos to year-on-year growth, even in the aftermath of the global financial crisis. Yet the country remains in the thrall of endemic corruption—a phenomenon which has undermined Russia's political and economic development, and threatens to cause long-term stagnation or even crisis.

According to the Transparency International “2012 Corruption Perceptions Index”, Russia ranks among the most corrupt developed countries in the world—133rd out of 176 countries surveyed, with the worst offenders at the bottom of the list.¹ According to Sergei Ignatyev, head of the Central Bank, this has cost the country \$49 billion in capital flight in 2012 alone.² In the West, corruption in Russia is often treated as a fact as unchangeable as the Russian winter—an assessment that is all-too-often informed by a patronising perception of the country as somehow naturally incompatible with building a law-abiding society. Others prefer to conveniently ignore the problems created by this endemic corruption, on the grounds of self-interest, rationalising that the money to be made from the energy and commodities sectors far outweighs the long-term economic; legal; or moral elements of this problem.

To view corruption as merely a problem for Russians is not only cynical, but also short-sighted. Ignoring this phenomenon enables the continuation of a system in which theft is not the exception, but the rule. In a globalised economy, and with the United Kingdom still struggling towards recovery, endemic corruption in one of the world's rising economic powers is a problem for the system as a whole, distorting competition and undermining the integrity of the financial sector.

While billions may be stolen in the Russian Federation, it does not usually remain in the country; it is swiftly transported through shell companies and accounts around the world, laundered in offshore entities as well as European Union countries such as Cyprus and Latvia, and legitimised through purchasing assets in global financial-centres such as London. Such funds can be rapidly put towards the purchase of reputational legitimacy via the financial and legal services of that country, or even the exercise of political influence.

This report explores the significance of Russian corruption, with particular emphasis on its impact and influence in the U.K. This is not to suggest that Russia is the only exporter of corruption with whom the U.K. should be concerned, as anti-corruption actions should clearly be universal in nature. The intent of this report is simply to highlight the fact that, given the significant amount of capital transferred to the U.K. from Russia, there is good reason for the U.K. to invest in fighting against the exportation of corruption, and to support efforts by Russian civil society to achieve meaningful reform. Such an effort has the potential not only to help the U.K. avoid the pitfalls associated with the injection of dirty money into the British economy, it can also perform a vital role in supporting efforts to reform Russia's economy and contribute to the fight against global corruption.

CHAPTER 1

CORRUPTION IN RUSSIA: RECENT HISTORY

Since the collapse of the Soviet Union, corruption has been one of the most pervasive and damaging problems afflicting the Russian Federation. As Russia transitioned from an authoritarian state with a centralised economy to a capitalist democracy, the breakdown of institutions made the country particularly vulnerable to corrupt activities. The lack of any meaningful lustration of the state security forces enabled the perpetrators of human-rights abuses to obtain positions of power and wealth in the post-Soviet era. Furthermore, the uncontrolled shift of wealth into a market economy; the uncertainty and missteps of the new political order; and the lack of a meaningful rule of law combined to embed corruption in the D.N.A. of the new political order.

The failure of institution-building, along with lax international scrutiny, severely distorted the process of privatisation in the immediate post-Soviet period, enabling a small group of businessmen—the oligarchs—to gain control of the commanding heights of the economy, as well as an enormous amount of political influence. One of the most significant examples of the fusion of political and economic corruption in the post-Soviet state was the infamous “loans-for-shares” arrangement of 1995-1996. Under this arrangement, Russia’s most powerful oligarchs lent money to the state as a pretext to recoup the loans through the purchase of shares in state-owned companies, at a price equal to thirty per cent of the difference between the market value of the shares and the amount lent to the government.

Throughout the 1990s, Western loans to Russia were funnelled into corrupt activities, and deposited in Swiss bank accounts. The extent of this practice was revealed in scandals, such as the infamous Bank of New York affair, in

which it was discovered that millions of dollars were being laundered through that bank throughout the 1990s.³ The easy availability of Western funds was also used to shore up the political position of the shambolic President, Boris Yeltsin, and his inner circle—known as “The Family.”⁴

Striking socioeconomic inequality reigned: by the time Boris Yeltsin left office in 1999, ten per cent of the population owned half of Russia’s wealth, and controlled much of the country’s political life.⁵ During this chaotic period, organised crime and business became intimately associated, with business disputes regularly settled through violence: in 1994, fifty bankers were assassinated in Moscow alone.⁶

Although pervasive corruption has plagued Russia since the Tsarist period, the mismanagement of the post-communist transition laid the basis for the re-emergence of authoritarianism under Vladimir Putin, and the marriage of public and private sector corruption under his personal authority. In his first presidential campaign in 2000, Putin ran against the lawlessness; conspicuous greed; and disproportionate political influence of the oligarchs—a popular stance to take in a country disgusted by the theft, excesses, and economic chaos of the 1990s. However, Putin quickly demonstrated that his intention was not to challenge this culture of corruption, but merely to bring it under the more centralised control of the state. “Like Yeltsin, Putin adopted corruption as a key element of his rule,” explained Russia specialist Mark Galeotti. “It’s how he co-opts people into the system, and gives him a carrot and a stick to use against the elite.”⁷ On 28 July 2000, Putin invited Russia’s most significant oligarchs to a meeting at the Kremlin, in which he communicated that they would be permitted to keep their wealth, provided that they committed to paying their taxes and staying out of politics.⁸ Those who were unwilling to accede to this arrangement—notably, Vladimir Gusinsky, Boris Berezovsky, and Mikhail Khodorkovsky—found themselves the subjects of criminal investigations, and saw their companies seized by the state and purchased by loyal Putin allies such as Roman Abramovich and Oleg Deripaska.⁹

Putin cemented his power base by installing loyalists from his time in both the St Petersburg mayoral office and the K.G.B. at the heart of government, and using the United Russia Party to dominate and transform the parliament into a “rubber stamp” authority. This new elite became known as the *siloviki*, or “strongmen”, and have been the enforcers and beneficiaries of the fusion of public- and private-sector corruption ever since. While the state and society contain numerous groups participating in corruption, the *siloviki*

are unique in their ability to wield power over the commanding heights of the economy, and to affect change through state-owned companies; the tax service; the security services; and the courts.¹⁰

Even at the local and regional level, politicians from, or allied to, the United Russia Party are found to have relatives with no prior commercial experience mysteriously entrusted with the running of hugely profitable enterprises, and civil servants on small salaries can be found to have sizeable assets, including expensive cars and property abroad. Analysts estimate Putin's own net worth to be up to \$40 billion—despite an official annual salary and military pension amounting to around \$148,000—¹¹ which he has been accused of amassing through illicit means.¹² “What we have in Russia is the merger of power and property,” commented Lilia Shevtsova, Senior Associate at the Carnegie Moscow Centre. “The men who rule Russia own Russia. They don't even need to bribe officials because they are the officials! So the key problem is how to divide this power, which is the basis for further transformation.”¹³

At the highest level, there is the political and economic corruption of graft; fraud; embezzlement; and kickback schemes generated through access to public funds. Government procurement contracts and infrastructure projects are among the most lucrative opportunities for corruption, with an estimated loss of \$32 billion per year through procurement alone.¹⁴ According to opposition politician and anti-corruption activist Vladimir Ashurkov, “[o]ne example we found at RosPil [Alexey Navalny's anti-corruption blog] was the practice of substituting Cyrillic letters on bids for government procurement with Latin letters which look the same, so that, when the information is published on the Internet, the search terms don't appear, limiting the competition so that you can make sure the tender is won by a particular company.”¹⁵

Massive corruption and the further deterioration of the rule of law have gone hand-in-hand with the steady erosion of democracy and human rights in Russia. While Dmitry Medvedev's presidency of 2008-2012 raised hopes among some Russians that genuine reforms might be underway, his promises to tackle corruption and “legal nihilism” proved largely insincere—as was his presidency (revealed in 2011 to have been a mere placeholder for the return of Vladimir Putin for a third term). The widespread electoral fraud displayed during the Duma elections of December 2011 was barely able to deliver a parliamentary majority to United Russia—partly a consequence of the party's widespread unpopularity and association with corruption. Putin

was re-elected in March 2012 with a convincing, but diminished, majority. The election was also marred by fraud, and was characterised by an overall absence of genuine political competition.

Corruption is the glue that holds together an unwieldy, vertically integrated system of power through elaborate, mostly unofficial, patronage. This phenomenon extends from the most senior officials and political allies within state-owned oil and gas companies like Gazprom and Rosneft, to the lower-level officials soliciting bribes to process permits for small business-owners. According to the “2011 Bribe Payers Index”, the country scores 6.1 on a scale of 10, with the majority of respondents believing police and public officials to be the institutions most affected by corruption.¹⁶ Political and economic corruption feed off one another, but perhaps the most significant element enabling the proliferation of both is Russia’s lack of judicial independence: in 2012, the country scored 6 out of 10 in Freedom House’s “2012 Judicial Framework and Independence Assessment.”¹⁷

Corruption acts as a double or triple tax on the Russian economy: first through theft; secondly, by depriving the state of tax revenue; and, in most cases, a third tax by leaving the country to be deposited in foreign countries. Thus far, the country’s economic health has been bolstered by the high price of oil and gas; yet there are increasing signs that the consequences of corruption could contribute to economic stagnation, or even crisis.

The overreliance on a largely state-controlled energy sector has left the economy vulnerable to future challenges, and struggling to diversify. The lack of competition within that sector, and the losses and inefficiencies bred by corruption, have left Russia particularly vulnerable to increased competition and any decline in the price of oil and gas. For example, while state-owned Gazprom has been the Leviathan of Europe’s energy market for the past decade, it is increasingly under threat—with an anti-trust investigation underway by the European Union, and an estimated 70 per cent value lost annually through corruption or waste, including billions spent on unnecessary pipelines.¹⁸

Political and economic corruption in Russia is thus deeply intertwined and mutually reinforcing, endangering the economy and undermining the country’s political development. Popular challenges to corruption are undermined by the lack of respect for individual rights, making corruption both an enforcer of political passivity and a galvanising issue for Russia’s burgeoning civil society.

ANTI-CORRUPTION ACTIVITIES IN RUSSIAN CIVIL SOCIETY

Political and economic corruption has emerged as one of the chief dissatisfactions of the Russian public, with 41 per cent of respondents in a November 2012 Levada Centre poll believing that corruption has increased over the past decade.¹⁹ The identification of United Russia with corruption is so significant that it has become popularly known as the “party of crooks and thieves”—a term coined by anti-corruption activist and opposition leader Alexey Navalny, and one of the rallying slogans of the 2011-2012 protest movement.

Navalny’s anti-corruption website, RosPil, has been instrumental in uncovering cases of corruption implicating members of Russia’s political and business elite, using novel investigative tactics—including the purchase of minority shares in state-run companies in order to draw attention to corrupt practices, and soliciting tip-offs from whistle-blowers. High-profile cases revealed by Navalny include allegations that Deputy Prime Minister Igor Shuvalov benefitted from oligarch Alisher Usmanov’s purchase of British steel company Corus Group (explored in a joint publication with the Russia Studies Centre),²⁰ and allegations of \$4-billion fraud during the construction of the 4,857-kilometre East Siberia-Pacific Ocean pipeline in 2006 by the Transneft oil-transport company.²¹

Navalny’s transformation into an internationally famous opposition leader has demonstrated the potential of corruption to become an impetus for political reform. As a consequence, Navalny is currently the subject of several criminal investigations accusing him of corruption—a Soviet-era tactic of attributing the crimes revealed by the whistle-blower to the whistle-blower himself. Among other allegations, Navalny has been accused of coercing the Kirovles timber company into entering into a loss-making deal;²² of defrauding an unnamed firm out of \$1.8 million in shipping charges;²³ and, most recently, of stealing \$3.3 million in funds from the now-defunct Union of Right Forces political party.²⁴

Navalny’s associates have also been targeted. On 7 February, Vladimir Ashurkov’s home was searched in connection to the latter probe; investigators seized documents, electronic equipment, and reportedly denied Ashurkov access to legal representation.²⁵ Nikita Belykh, the liberal governor of the Kirov region, has been accused of stealing \$3 million in state property; subjected to a no-confidence vote by Kremlin proxies within the regional government; and has also been questioned in relation to the investigation

into Alexey Navalny.²⁶ Fellow oppositionists Leonid Gozman, Boris Nemtsov, and Maria Gaidar have also been questioned in relation to this alleged theft, in what is widely seen to be a pretext for the harassment of key members of the Russian opposition.²⁷

Following Navalny's strategy, Russia's protest movement has increasingly focused on anti-corruption efforts. Eduard Mochalov, a farmer-turned-muckraking journalist based in the province of Chuvashia, publishes a monthly free newspaper called *Vzyatka (The Bribe)* detailing the activities of the corrupt officials who steal from Chuvashia's regional coffers, and has been cited by Navalny as a promising example of grassroots activism.²⁸ Other opposition leaders, including Boris Nemtsov and Vladimir Milov, have also campaigned for transparency and the reform of the corrupt nexus between the state and private sectors in Putin's Russia.

Anti-corruption activists face numerous challenges, including a cultural environment of political passivity in which corruption is accepted by many as the price of doing business. "Anti-corruption is a growing sentiment, but it is still controversial in traditional locations where it is an easy way to solve problems," explained Lilia Shevtsova. "You pay a bribe to the officials, to the police, to the school to get your kid into kindergarten. It can help the local population to quickly solve some of their problems, but the level of corruption is becoming so global, it's everyone's problem now."²⁹

While corruption is consistently shown to be the issue most capable of arousing public anger in Russia, widespread political passivity and the weakness of civil society have made it difficult for anti-corruption activists to translate these sentiments into a sustained campaign for reform. However, corruption has clearly been identified as a threat to the stability of the current regime, which is currently engaged in an attempt to neutralise the political potency of this issue.

THE GOVERNMENT'S ANTI-CORRUPTION DRIVE: POTEKIN POLITICS OR SERIOUS INITIATIVE?

The Russian government is not oblivious to the economic and political challenges posed by corruption, which is one of the reasons why it has launched a public campaign to reduce corruption. In light of the worsening authoritarianism in Russia, and the country's record of paying lip service to international standards without meaningful enforcement, the substance of these initiatives is doubtful.

In the past, anti-corruption measures such as anti-money-laundering regulations (A.M.L.) have been adopted in reaction to widespread international pressure, but they are rarely—or only selectively—enforced. Russian A.M.L. legislation makes reference to the Financial Action Task Force (F.A.T.F.) “Forty Recommendations”, and the “Wolfsberg Principles” (the industry-drafted standards for oversight and best practice) are recognised by the Russian banking community.³⁰ Despite incorporating these measures into Russian law, Russia’s judicial system does not tend to prosecute cases of professional money-laundering involving organised crime. While this could be attributed to a lack of resources to detect complex money-laundering schemes, the Russian law enforcement’s objectivity and incentives in relation to these matters is questionable.³¹ Instead, anti-corruption measures are largely held to be used selectively against political opponents, rather than to seriously combat the problems which most plague the Russian Federation. Barriers to enforcement of anti-corruption measures are solidified by the de facto immunity granted to key Russian officials, including the President; members of Parliament; judges; jurors; and local-government officials.³²

Since late 2012, both Putin and Medvedev have publicly affirmed the government’s dedication to both anti-corruption efforts and political reform. In February, Russia’s Interior Minister, Vladimir Kolkoltsev, announced that the police had investigated 45,000 corruption crimes over the past year, and that criminal proceedings have been initiated against 10,000 individuals.³³ Legislative initiatives have formed a significant part of this government campaign, in what is widely believed to be an attempt to present an image of compliance with Organisation for Economic Co-operation and Development (O.E.C.D.) recommendations in support of Russia’s bid for O.E.C.D. membership.³⁴ This was the motivation behind Russia’s decision to sign on to the O.E.C.D.’s “Anti-Bribery Convention” in 2012.³⁵

In January 2013, a law came into force requiring the rotation of civil servants, with the aim of reducing the opportunity for public servants to engage in corruption.³⁶ The most high-profile of these new legislative initiatives has been a bill, introduced by Putin, banning federal and regional officials; senior prosecutors; board members of the Central Bank; and employees of state corporations from holding foreign bank accounts; bonds; and shares, and from using family members as proxies for these practices.³⁷ Similar measures were passed during Medvedev’s presidency; but proved toothless, as officials routinely put their assets in the names of family members or other proxies. In the case of the most recent bill, there is good reason to be sceptical about

whether the provisions will or can be enforced, as there is little incentive to keep wealth in Russia, given the lack of protection for private property.

United Russia Duma representative Vladimir Pekhtin has resigned in response to an investigation into allegations that he holds assets in the United States—allegations first made by Alexey Navalny.³⁸ In another ironic example of the government following Navalny's lead, Putin has also called for the public oversight of the utilities sector, following the success of Navalny's campaign encouraging people to send him complaints of poor utilities.³⁹

It is likely that, as with other anti-corruption efforts, these measures will go on the books but will not be enforced. In fact, it is more likely that this issue will be used as a cover for the purge of high-level officials; to settle scores; and to instil fear in the country's political elite. The dismissal of former Defence Minister Anatoly Serdyukov is perhaps the clearest example of this practice.

FACT BOX: THE SERDYUKOV CASE

In November 2012, Putin fired Serdyukov following the opening of a criminal investigation into his alleged theft of between \$100 million and \$200 million through the sale of undervalued assets, and the awarding of army procurement contracts to friendly businesses by Oboronservis, the ministry-owned military-property company.⁴⁰ Serdyukov was already an unpopular figure within the military, and it has even been suggested that his dismissal may also have been a matter of personal loyalty: Serdyukov is alleged to have been unfaithful to his wife, who is the daughter of Putin's mentor, the former Prime Minister Viktor Zubkov.⁴¹ To date, three officials working under Serdyukov have been charged in connection to the fraud, as has his presumed mistress, Yevegeniya Vasileyva, and a minimum of five more are expected to be charged in due course.⁴²

These revelations came amidst reports by Transparency International concluding that Russia's defence sector is among the most corrupt in the world, earning a "High Risk" rating, in common with Turkey; Belarus; and China.⁴³ Yet, according to Mark Galeotti, "[h]owever dramatic the Oboronservis case may be [...] it represents only a fraction of the total embezzlement from the military, which Military Prosecutor General Sergei Fridinsky has estimated tops \$10 billion a year."⁴⁴

Since late 2012, other arrests and announcements of investigations across Russia's public sector include the following cases:

- In August 2012, the Interior Ministry launched an international investigation into Yelena Kotova, a former member of the board of directors of the European Bank for Reconstruction and Development, on charges of seeking a bribe.⁴⁵ The investigation into Kotova implicated a British oil-and-gas group, Vostok Energy, over accusations of involvement in bribery and corruption. Kotova is also under investigation by London police in relation to these charges.⁴⁶
- In November 2012, the chief architect of Russia's G.L.O.N.A.S.S. satellite navigation system, Yury Urlichich, was dismissed following accusations that he had embezzled \$200 million—prompting Russia's Deputy Prime Minister to warn of a “clean-out” of corrupt state officials.⁴⁷
- Also in November, former Agriculture Minister Elena Skrynnik was accused of embezzling \$20 million from the state-controlled leasing company O.A.O. Rosagroleasing, and was accused by state television of involvement in a \$1.3 billion fraud.⁴⁸
- In December 2012, former federal official Anatoly Shesteryuk was arrested on charges of stealing \$330 million in property from the Federal Property Management Agency.⁴⁹
- In February 2013, an investigation into the embezzlement of millions of dollars earmarked for Medvedev's pet project, the Skolkovo Innovation Centre, was launched.⁵⁰
- Also in February, Putin fired Akhmed Bilalov, the deputy president of the Russian Olympic Committee, for mismanagement. Inflated construction costs and property prices as a consequence of corruption are already estimated to have cost \$37 billion—only \$3 billion less than the record-breaking Beijing Olympics.⁵¹

The lack of any attempt to undertake the types of systemic reforms needed to challenge Russia's culture of corruption—namely, the meaningful application of the rule of law; judicial independence; government transparency; the end to censorship; and the introduction of genuine political competition—indicates that such anti-corruption efforts will be insufficient, if not merely tokenistic. While Putin and Medvedev have professed their commitment to

democratic reforms, the marked increase in authoritarian measures rushed through the state Duma since the return of Vladimir Putin as President in May 2012 has belied the declared programme of political and legal reform. Increasing signs of authoritarianism have included escalated fines for unauthorised protest, an expanded treason law with enhanced prison sentences, and increased restrictions on Internet content.

Ultimately, the greatest obstacle to genuine anti-corruption reform is the system itself. “There is no possibility of genuine anti-corruption reform because this would require the rejection of the elite’s monopoly on power, and the introduction of economic and political competition,” reasoned Lilia Shevtsova.⁵² Mark Galeotti put it more starkly: “If Putin woke up tomorrow and said ‘we’re going to fight corruption’ and actually meant it, he would be declaring war on everyone who keeps him in power.”⁵³

CORRUPTION AND HUMAN RIGHTS IN RUSSIA: TWO CASE STUDIES

Pervasive corruption needs two main elements to survive: a complicit or passive political leadership, and a breakdown in the rule of law. The casualties of this phenomenon rarely remain confined to the economic sphere, as the individuals who compromise or challenge corruption become problems to be solved within an amoral setting. Indeed, the same conditions which produce human-rights violations—the absence of the rule of law and civil liberties—are also the conditions which enable the proliferation of corruption. Over the past decade, two cases have achieved almost totemic significance in illustrating the connection between corruption and systemic disrespect for human rights: the almost-ten-year incarceration of former Yukos oil company C.E.O. Mikhail Khodorkovsky, and the imprisonment and murder of the anti-corruption attorney, Sergei Magnitsky.

MIKHAIL KHODORKOVSKY: “THE WORLD’S BIGGEST THREAT IS CORRUPTION, NOT NUCLEAR WEAPONS”

The prosecution of Yukos executives Mikhail Khodorkovsky and Platon Lebedev, and the state expropriation of the multi-billion-dollar company represented a turning point in the assertion of Putin’s power monopoly, demonstrating the close connection between state corruption and disrespect for human rights.

Yukos was purchased by Khodorkovsky during the loans-for-shares scheme of 1995-1996. Between 1999 and 2000, Yukos became the first Russian company to adopt Western standards of corporate governance; transparency; and shareholder rights. These measures were intended to attract increased foreign investment and transform Yukos into a global company, and proved extremely successful. Mikhail Khodorkovsky became the richest man in Russia, and one of the most politically powerful forces in the country, and spearheaded projects promoting democratic reforms. He quickly established himself as an enemy of Putin when he refused to cease his political activities and directly accused the government of corruption.

In July 2003, Lebedev, C.E.O. of the Yukos holding company, Group Menatep, was arrested on charges of embezzlement, followed by Khodorkovsky on 25 October 2003 on charges of tax evasion; fraud; and embezzlement. The Prosecutor's Office froze 44 per cent of Yukos' shares—an unprecedented action in post-Soviet Russia. The state successively increased its charges against Khodorkovsky and Lebedev to multiple counts of fraud and theft through corporate-tax accounting schemes which Yukos—in common with almost every other large-scale Russian company—had employed in order to minimise its tax liability. Khodorkovsky and Lebedev's trial began in June 2004, and the pair were convicted and sentenced in 2005 to nine years imprisonment in a Siberian labour camp.

Shortly before Khodorkovsky and Lebedev were to become eligible for parole, new charges were lodged and a second trial was held in 2009, and, following a failed appeal in 2011, both men's sentences were extended to 2016. Lebedev and Khodorkovsky have been designated prisoners of conscience by Amnesty International, and their trials have consistently failed to meet international standards of justice. Additionally, former Yukos vice-president, Vasily Aleksanyan, was imprisoned from 2006 to 2009, and his death in 2011 from an A.I.D.S.-related illness is widely thought to have been hastened by the poor conditions of his incarceration.

Yukos was stripped of its assets, and, in 2004, the Russian government forced through the auction of Yukos' most important subsidiary, Yuganskneftgaz. (It is widely suspected that the same government then orchestrated a scheme to purchase the subsidiary through a front company). Multiple claims by stockholders and other relevant parties have been brought against the Russian government in international courts, including the European Court of Human Rights. The Russian government continues to hound those associated with Yukos, using all the tools available to it in the international

system—including extradition requests; the abuse of Interpol warrants; and the pursuit of asset freezes.

The case became a turning point in illustrating the lengths to which Putin and his allies would go in order to secure their monopoly on power, as well as the turn away from even the pretence of judicial independence and rule of law towards “telephone justice”—the colloquial term for the practice of officials instructing judges of the appropriate verdict. In the process, two men have remained in prison for almost ten years, and become living symbols of the extent to which the imperatives of corruption trump the rights of the individual in Putin’s Russia.

SERGEI MAGNITSKY: SILENCING THE WHISTLE-BLOWER

Sergei Magnitsky’s belief in the Russian legal system’s ability to provide remedy for injustice persuaded him to go public with evidence implicating state officials in the theft of \$230 million in fraudulent tax refunds. After refusing to rescind his charges, he was framed for the crime that he had uncovered, and imprisoned. He died in agony after a year of medical neglect and suspected abuse at the hand of his captors.

On 4 June 2007, a Russian Interior Ministry police unit raided the offices of Hermitage Capital Management and Hermitage’s law firm, Firestone Duncan, where Sergei Magnitsky worked as an attorney. The police unit, led by Lt Col Artem Kuznetsov, claimed to be investigating a possible tax fraud related to one of Hermitage’s client’s companies, seizing documents—including the corporate seals of many of Hermitage’s investment companies.

Magnitsky was charged with investigating the case. He uncovered evidence that documents seized from Hermitage’s and Firestone’s offices were now being used by state officials to execute a convoluted scheme, whereby an invented tax liability against fraudulently registered subsidiaries of Hermitage was used to secure a tax refund of \$230 million. The \$230 million was processed within forty-eight hours, and wired to several banks in Moscow—including Universal Savings, which was owned by Dmitry Klyuev, the alleged head of the Klyuev crime syndicate—before leaving Russia to be laundered through several international banks. (Parliamentary representatives were reportedly shocked when Klyuev arrived at the Organisation for Security and Co-operation in Europe (O.S.C.E.) venue in July 2012 while they were conducting a hearing on his alleged involvement in the Magnitsky fraud).⁵⁴

In July 2008, Magnitsky and Hermitage filed criminal complaints, and the Interior Ministry responded with investigations into all of Hermitage's attorneys at Firestone Duncan. Hermitage C.E.O. Bill Browder, offered to relocate his attorneys from Russia, but Magnitsky refused and testified before the Russian State Investigative Committee, naming Kuznetsov and Interior Ministry official Pavel Karpov as the orchestrators of the fraud. A few months later, Magnitsky was arrested and detained on the charge of acting as the director of two Hermitage companies that had allegedly failed to pay taxes in 2001.

Magnitsky was subjected to physical and psychological torture in prison, and was pressured to confess to stealing the \$230 million and to blame Browder for tax fraud, but refused. He was denied medical care during his 358 days in jail, and, in July 2009, was diagnosed with calculous cholecystitis. Despite a recommendation for transfer from the Matrosskaya Tishina prison in Moscow to alternative facilities with emergency medical capabilities, this request was denied—as were Magnitsky's numerous petitions for medical treatment and a fair hearing. He was instead moved to the infamous Butyrka prison, formerly the home of political prisoners in the Stalinist period, where he was diagnosed with acute pancreatitis.

Magnitsky died on 16 November 2009, at the age of 37, in excruciating pain. His death is thought to have been hastened by a beating with batons that he had sustained hours prior to expiring. There followed a cover-up of the cause of Magnitsky's death by the prison authorities, with the Public Oversight Commission concluding that “[a]n ill person in severe condition was effectively left without medical attention (for 1 hour 18 minutes) to die in an isolation ward.”⁵⁵

Russia's *New Times* uncovered evidence that officials within the state security services and the Interior Ministry had collaborated to frame Magnitsky, receiving a \$6 million payoff.⁵⁶ Incredibly, Kuznetsov was appointed to head of the investigation into the fraud, which resulted in only token sentences handed down to Viktor Markelov and Vyacheslav Khlebnikov.⁵⁷ To date, none of the officials implicated in the tax fraud have been punished—in fact, several have been promoted.

SERGEI MAGNITSKY'S DEATH: INTERNATIONAL IMPACT

Magnitsky's death and the apparent cover-up provoked outrage around the world. However, demands from domestic and international human-

rights groups and Russian opposition leaders for a full and transparent investigation have been ignored. Browder's multi-national lobbying effort to convince democratic parliaments to impose sanctions on the sixty Russian officials involved in the conspiracy has resulted in the passage of the "Sergei Magnitsky Rule of Law Accountability Act" by the U.S. in December 2012, imposing asset freezes and travel bans on the individuals implicated in Magnitsky's imprisonment and death, as well as any other Russians credibly suspected of human-rights abuses.

The effect of this new legislation has been electric. After a strenuous lobbying effort to convince U.S. lawmakers to scrap the Bill, the Kremlin's hysterical reaction to the "Magnitsky Act"—including a retaliatory law banning U.S. officials from owning assets in Russia and, bizarrely, banning U.S. citizens from adopting Russian children—has demonstrated just how significant a threat this legislation is to the current power structure. By limiting the opportunities for the participants in corruption to spend their profits and/or relocate abroad, the "Magnitsky Act" chips away at the bonds which hold together Putin's vertical structure of power.

The passage of the "Magnitsky Act" in the U.S. has thrown down the gauntlet for other countries. Indeed, these types of limited sanctions are the best way of punishing illegal and immoral behaviours without hurting the Russian people—and, in fact, of demonstrating solidarity with the Russian people. The expansion of the "Magnitsky List" to other human-rights abusers is already under discussion, and suggestions of additions include the Chechen dictator, Ramzan Kadyrov,⁵⁸ as well as individuals implicated in the unfair trials of the Yukos executives, and individuals suspected of involvement in the murder of journalist Anna Politkovskaya.

In October 2012, the European Parliament recommended that the Council of Europe impose sanctions against the individuals suspected of culpability in Magnitsky's imprisonment and death. In Canada, Irwin Cotler MP proposed legislation similar to the U.S. "Magnitsky Act", and, in March 2012, a motion was unanimously passed by the U.K. House of Commons calling on the government to impose visa sanctions and asset freezes for those involved in the Magnitsky case. Resolutions, recommendations, and declarations regarding the Magnitsky case have also been passed by the U.K.; Holland; Poland; Italy; the O.S.C.E.; and the Parliamentary Assembly of the Council of Europe.⁵⁹ If replicated by other countries—and particularly by members of the E.U.—the Act has the potential to seriously undermine the Russian regime's ability to command loyalty via the patronage obtained through corruption.

Numerous investigations into the \$230-million tax fraud are currently underway, while the Russian government has proceeded with the unprecedented posthumous trial of Sergei Magnitsky in Moscow's Tverskoi court on charges of tax evasion. An on-going investigation by the Organized Crime and Corruption Reporting Project,⁶⁰ working together with *Barron's* and *Novaya Gazeta*, has uncovered documentary evidence tracing \$134 million of the funds through banks in the Ukraine; Kyrgyzstan; Moldova; Latvia; Lithuania; Estonia; and Cyprus via shell companies registered in the U.K.; British Virgin Isles; and Belize, as well as evidence of the involvement of organised crime.⁶¹ The investigators have alleged that the stolen funds can be linked to apartments paid for by Vladlen Stepanov—the ex-husband of one of the tax officers who executed the fraud—and Denis Katsyv, the son of Moscow Region's former transportation minister.⁶² As a result of evidence provided to Swiss prosecutors by businessman Alexander Perepilichny (who died in November 2012 under mysterious circumstances), Switzerland; Cyprus; Latvia; Moldova; and Lithuania have all launched investigations into the locations of these stolen funds.⁶³

CHAPTER 2

RUSSIAN CORRUPTION: A DOMESTIC AND INTERNATIONAL PROBLEM

Corruption has significantly undermined Russia's economic development, the consequences of which are only likely to become clear over the next decade. An estimated \$211.5 billion in illicit capital outflows left the country between 1994 and 2011 (according to the Global Financial Integrity organisation, which it describes as the "proceeds from crime, corruption [and] tax evasion").⁶⁴ Studies indicate that bribes paid in order to obtain privileges—such as an investment license—reduce the incentives for entrepreneurialism, and discourage Foreign Direct Investment (F.D.I.).⁶⁵ This environment is thought to contribute substantially to the emigration of young professionals: over 2.5 million people left Russia over the past decade, suggesting that corruption is also encouraging significant brain drain.⁶⁶

Russian corruption also affects both international and domestic security. The links between organised crime; politics; and corruption in Russia are well established, with Russia's state security agencies suspected of using organised crime to carry out criminal operations, and of providing protection to crime syndicates in turn, according to the Wikileaks cables released in 2010.⁶⁷ This is one of the reasons why Russia is popularly referred to as a "mafia state." More recently, there have been allegations regarding the role of organised crime in the \$230-million tax fraud uncovered by Sergei Magnitsky (referenced in the previous chapter). "Organised crime and politics are depressingly interconnected in Russia," said Mark Galeotti. "They create the networks that facilitate the corrupt money. You can be a political figure and a criminal lynchpin—these are not boundaries that matter."⁶⁸

Russian organised crime is a significant challenge to the E.U. as a whole, where

it is a key player in the drugs trade and human trafficking throughout Europe, as well as in orchestrating fraudulent schemes and money laundering. These organised-crime syndicates have also been linked to Russian businessmen who, a U.S.-government report alleges, use crime syndicates to “[...] collude with state or state-allied actors to undermine competition in strategic markets such as gas, oil, aluminium, and precious metals.”⁶⁹ Protection money, or *krysha*, is routinely paid to organised-crime syndicates by some of the most lucrative and high-profile companies in Russia. For example, in the recent legal dispute between aluminium magnate Oleg Deripaska and billionaire businessman Michael Cherney, Deripaska admitted that he had paid *krysha* to organised-crime figures linked to Cherney in order to protect his business interests.⁷⁰

As a world power with a seat on the Security Council, endemic corruption at the heart of Russian government poses an obvious problem to the conduct of world affairs—as has been demonstrated by the material and diplomatic support Russia has provided to the murderous Assad regime throughout the Syrian civil war. Moreover, as Vladimir Ashurkov points out, “[t]he first concern to the U.K., and to any country, should be the impact that corruption has on security, because corruption permeates the military, and dangerous information and materiel can fall into the wrong hands.”⁷¹ This is a particularly significant concern, given the fact that Russia is a nuclear power. In relation to international co-operation on the illegal arms trade and terrorism, the well-established links between government officials and the infamous arms-dealer, Viktor Bout,⁷² underscores the way in which corruption so easily bleeds into activities with harmful or deadly consequences in the name of greed.

Corruption is not new to Russia, nor is it unique, but, as Mark Galeotti explained, “Russian corruption is unique in terms of the stage Russia is at in its global development.”⁷³ As much as corruption primarily impacts the Russian people, it also undermines the global economy, and devalues the rule of law and the rules-based financial system on which economic stability depends.⁷⁴ In addition to the diffuse and unaccounted-for funds obtained through corruption flooding the international system, corrupt or questionable business practices exported into the international market from Russian businesses or banks also undermine the stability and security of the international financial system (as highlighted in the report co-written by the Foundation for Fighting Corruption and the Russia Studies Centre, examining the practices of V.T.B. Bank).⁷⁵ The U.K.’s sophisticated regulations and robust legal system mean that it is better protected from the destabilising effects of corruption than smaller countries. However, the exportation of these

practices is a challenge which requires vigilance.

THE U.K. REGULATORY LANDSCAPE: RUSSIA AND THE EXPORTATION OF CORRUPTION

The U.K. has a robust legal- and parliamentary-system, with a proven record of serious commitment to enforcing the rule of law in relation to corruption and financial crime. The system relies upon the F.S.A. to formulate regulations concerning financial crime; upon the government to sponsor primary legislation and define criminal offences; upon law-enforcement agencies, including the Serious Fraud Office (S.F.O.) and Serious Organised Crime Agency (S.O.C.A.—set to be incorporated into the new National Crime Agency in 2013); upon the courts to adjudicate these matters; and upon the co-operation with the domestic agencies of other countries (such as the U.S. Security and Exchange Commission), as well as with regional and international organisations such as Europol or Interpol.

Anti-money-laundering (A.M.L.) measures are among the most important tools in fighting corruption within the U.K. and, particularly, corruption exported from countries like Russia. A.M.L. legislation has undergone a period of significant development over the past three decades. Money-laundering offences were initially covered by the “Drug Trafficking Offences Act (1986),” and later the “Drug Trafficking Act (1994).” New offences were introduced under the “Criminal Justice Act (1993)” in order to address the proceeds of non-drugs-related crime, and the scope was extended again in 2002 with the passage of the “Proceeds of Crime Act (P.O.C.A.),”⁷⁶ which consolidated the criminal treatment of money laundering.⁷⁷ Money-laundering regulations were further articulated in the “Money Laundering Regulations Act (2007),” and the “Transfer of Funds Regulations (2007),” and are outlined in the F.S.A. handbook.⁷⁸

The F.S.A. relies primarily upon the banking sector to police suspicious activities through rigorous “know your customer” procedures and the submission of “Suspicious Activities Reports” to the F.S.A. Transparency International has reported that up to 200,000 “Suspicious Activities Reports” are received each year by the U.K. Financial Intelligence Unit (U.K.F.I.U.) within S.O.C.A.⁷⁹ However, despite improvements in compliance practices over the past decade, the F.S.A. has found that approximately one third of banks surveyed, including the private-banking arms of some major banking groups, “[...] appeared willing to accept very high levels of money-laundering

risk if the immediate reputational and regulatory risk was acceptable.”⁸⁰ In essence, a culture prevails in which banks are happy to accept high-risk clients if they think they can get away with it in the court of public opinion. The 2011 F.S.A. report noted that approximately one third of the banks in their sample discounted serious allegations against customers when criminal charges were unlikely to be brought forward, with almost half of the banks surveyed accepting information provided by customers “[...] at face value.”⁸¹ Moreover, three quarters of the banks surveyed “[...] failed to take adequate measures to establish the legitimacy of the source of wealth and the source of funds to be used in the business relationship.”⁸²

The identification of risks associated with “Politically Exposed Persons” (P.E.P.s—defined as a current or former foreign political figure, their immediate family, and/or close associates) has improved in recent years. However, the level of risk assessment undertaken by financial intermediaries remains questionable and has been criticised by the F.S.A., which found that some banks do not even have formal procedures to assess P.E.P.s.⁸³

The F.S.A. further criticised banks for failing to implement robust risk-assessment practices in relation to clients, and for inadequate due diligence procedures. In relation to foreign-born customers, the F.S.A. noted its discomfort with the fact that “[...] some banks placed undue reliance on the fact that some customers held investment visas”, noting that “[...] investment visas are allocated on the basis of funds held in regulated financial institutions anywhere in the world; they are not an indication of the customer’s integrity or the quality of A.M.L. controls in the jurisdiction where the funds are held.”⁸⁴

Additionally, there is the challenge of policing money deposited in U.K.-controlled tax havens such as the Channel Islands and British Virgin Islands, in which laundered funds are relatively easy to hide through shell companies. For this reason, the U.K. has been described as “offshore, onshore,” as it has among the most stringent financial regulations in the world, but remains vulnerable to financial crime due to problems of enforcement and its general attractiveness to the carriers of dirty money.⁸⁵ Transparency International’s conclusions reinforced the F.S.A.’s concern that it is all-too easy to shroud the wealth derived from corrupt or questionable sources in complex structures such as anonymous and/or offshore trusts and companies.

Anti-corruption N.G.O.s such as Transparency International have been critical of the U.K.’s handling of financial crime, pointing out the need for a more “[...] coordinated, proactive approach” that identifies and focuses on

countries that require assistance with investigations into financial crime.⁸⁶ While the U.K. has imposed steeper fines for this type of activity in recent years, it is (according to insiders) the public exposure of these practices that tends to be more effective than fines, as this generates negative publicity and undermines customer confidence.

Financial crime has been dealt with more severely over the past decade, since the U.K. was revealed to have been a major conduit of laundered funds for terrorism after the “September 11” attacks. Revelations of the numerous scandals in the banking sector

following the 2008 financial crisis have also bolstered the emphasis on effective financial regulation. The passage of the U.K. “Bribery Act” in 2010 has also strengthened the existing legislative framework for dealing with both domestic and international corruption, notably by introducing a strict liability offence for companies and partnerships which fail to prevent bribery.

It is clear that the regulatory and legislative framework for countering and punishing financial crime in the U.K. is strong. However, more could be done to improve enforcement, and to pressure banks to improve their policing efforts of high-risk clients.

WHY SHOULD THE U.K. WORRY ABOUT RUSSIA?

An estimated 300,000 Russians reside in the U.K., with a small, but significant, proportion of those migrants in possession of substantial wealth. According to the *Daily Telegraph*, one hundred Russian millionaires accounted for a quarter of the Tier-1 U.K. visas issued in 2012—demonstrating the attraction of London as a destination for Russia’s wealthiest, including oligarchs such as Roman Abramovich; Eugene Shvidler; and Boris Berezovsky.⁸⁷ “You can get a Tier-1 visa with a £1-million investment, and the default position of the government is to let you in,” Mark Galeotti noted. “As long as there’s reasonable doubt, unless you are a known criminal they’ll let you in—so you can essentially buy British residence in this way.”⁸⁸ This does not include the wealthy Russians who own property and other assets in the U.K. or in U.K.-controlled offshore territories such as the Channel Islands and British Virgin Islands.

While most Russians residing in the U.K. have earned their money perfectly legitimately, the nature of Russian business, and particularly businesses with direct and close connections to the Russian state, is such that the U.K.

has an interest in establishing the legitimacy of that wealth. In addition to the U.K.'s domestic interest in protecting its financial integrity, there are significant reasons for the U.K. business community to be concerned with Russian corruption. The U.K.'s lucrative energy sector, in particular, should be mindful of the risks inherent in dealing with endemic corruption, even if the potential profits may appear to outweigh such concerns—as was demonstrated, for example, by the accusations of corruption within the joint U.K.-Russian venture, T.N.K.-B.P.⁸⁹ “You might think that what happens in Russia doesn’t affect the U.K., but we’ve seen the shenanigans with oil and B.P.,” Mark Galeotti pointed out. “This is an economic field with which we want to interact. And their mind-set is that the rules of the game are meant to be circumvented. That affects Britain in any market.”⁹⁰

The attempted murder of Russian businessman German Gorbuntsov in Canary Wharf in March 2012 suggests the way in which the lawless practices of Russian business can directly impact the U.K. Gorbuntsov maintains that this attack was undertaken to prevent him from giving evidence to Russian prosecutors relating to an assassination attempt on his former business partner, Alexander Antonov, in Moscow in 2009, which inspired Gorbuntsov to flee to the U.K. in 2010. He further alleges the people responsible for the attempt on his life are affiliated with Putin.⁹¹

Alexander Perepilichny, a Russian private banker who assisted Swiss prosecutors in their investigation into the tax fraud uncovered by Magnitsky, was found dead outside his Surrey home on 10 November 2012, three years after fleeing to the U.K. The cause of death remains unknown, but at the age of 44, with no known health problems, many suspect that Perepilichny was murdered as retribution for his role in exposing the perpetrators of the Magnitsky fraud.⁹² Perepilichny was also reportedly warned in 2011 that his name had been found in the hit list of a Moscow gang.⁹³ It is the fourth mysterious death related to the Magnitsky case.

The investigation into the cause of Perepilichny’s death remains ongoing, but if evidence of foul play is discovered, the consequences of Russian corruption will have had a direct and dangerous effect on the U.K. According to Bill Browder, who contacted the Surrey police several times to stress the context of Perepilichny’s death and its potentially explosive implications, the police have not handled the case accordingly.⁹⁴ If this is true, this oversight must be redressed: such a revelation would have particularly serious implications for U.K.-Russian relations, already strained as a result of the poisoning of

the dissident and British citizen, Alexander Litvinenko, in London in 2006. According to Dominic Raab MP, who sponsored the motion calling on the U.K. government to impose visa sanctions and asset freezes for those involved in the Magnitsky case, “[t]he Perepilichny case is highlighting the problem posed to this country by Russian corruption, and the significance of the Magnitsky case to the U.K.”⁹⁵

The suspicions raised by Perepilichny’ s death evoke memories of the mysterious demise of British attorney Stephen Curtis in a helicopter crash, a few months after the arrest of his client, Mikhail Khodorkovsky. Curtis had been participating with a money-laundering investigation by National Criminal Intelligence Service into Russian business activity in London, and had received threats on his life in the weeks prior to his death. While the investigation into the crash uncovered no credible evidence of sabotage, the circumstances surrounding Curtis’ death remain suspicious.⁹⁶

It is clear that the U.K. must be mindful of the exportation of corruption from anywhere in the world, and will always fight an uphill battle, given the attractiveness of London as a financial centre, and the innate difficulties entailed in tracking and uncovering dirty money. However, the substantial links between the U.K. and Russia, and the crime associated with Russian corruption should make countering Russian corruption of particular interest to the British government.

CHAPTER 3

RECOMMENDATIONS

Russia's corruption problem requires a systemic solution—specifically, the meaningful application of the rule of law; judicial independence; government transparency; an end to censorship; and the introduction of genuine political competition. Such reforms must come from within Russia, and there is little the international community can or should do to become directly involved in this domestic struggle. However, countries like the U.K. can bolster anti-corruption reforms in Russia by limiting the options for the exportation of corruption, and highlighting the activities and plight of Russia's anti-corruption activists. For the U.K., any of the four following initiatives could significantly help in this effort.

IMPROVED DOMESTIC ENFORCEMENT

The first step in any anti-corruption effort must be to ensure that one's own house is in order. The U.K.'s banking sector has been criticised for being overly process-oriented in their approach to compliance with the financial regulations meant to guard against corruption, and for failing to invest the resources necessary to ensure that these measures are fully implemented. The F.S.A. itself has also been criticised for failing to take robust action against organisations which have failed to uphold their regulatory duties.

Investment in the Serious Fraud Office (S.F.O.) should be a key plank of any serious attempt to stem corruption. Planned budget cuts to the S.F.O. should be reconsidered: the department has experienced sharp cuts over the past four years, operating on a mere £33 million in 2012, and set to be reduced to £29 million over the next two years.⁹⁷ Indeed, a regular complaint by

law enforcement is that the government fails to support financial policing with the requisite resources. Clearly, there are areas which urgently require austerity measures and efficiency overhauls within the government, but the paltry funds allocated to this key enforcement arm do not bode well. According to Vladimir Ashurkov, “We have submitted a number of dossiers of information to the S.F.O. and F.S.A., drawing their attention to various cases of bribery or fraud, but haven’t heard anything yet. We understand that the S.F.O. is overstretched, and law enforcement is overstretched, but at a certain point, this becomes a matter of political will.”⁹⁸

Measures which could be taken by the relevant governmental bodies to improve enforcement include: ensuring awareness by the business community of the risks involved in doing business in Russia; encouraging those companies which engage with Russia to lead by example; and rigorously monitoring and punishing companies that support corruption by paying bribes. More must be done to draw attention to Western companies, politicians, and individuals who directly or indirectly serve the interests of the Russian elite—and thus help to prop up a system that is robbing its populace, and impinging upon their personal freedom. As Lilia Shevtsova has argued, “When the business community agrees to obey the rules of the game proposed by the Russian elite, it has to own up to the fact that it is indirectly supporting the system.”⁹⁹

The U.K. “Anti-Corruption Champion” is another platform which can be used to draw attention to this issue, and is currently occupied by the Secretary of State for Justice, Chris Grayling. The government should clarify the remit and purpose of this role, as has been requested by the Anti-Corruption All-Party Parliamentary Group.¹⁰⁰

On a Parliamentary level, U.K. policymakers should do more to acquaint themselves with the work and challenges faced by grassroots anti-corruption activists in Russia, whose operations have been increasingly constrained as a result of the Russian government’s crackdown on N.G.O.s, and its pseudo-legal harassment of any individuals seen to be opposed to the government.

ENHANCED PUBLIC SCRUTINY

According to Sir Ian Andrews, Chair of S.O.C.A., “[t]he U.K. ‘Bribery Act’ represents the most radical anti-corruption legislation in the world, but we need others to follow suit [...] all stakeholders must work seamlessly together, aided by a free press. Public scrutiny is the best tool.”¹⁰¹ Libel reform is a

tangential, but no-less influential component in the successful fight against both domestic and international corruption. The free press provides a vital means of support for the activists and ordinary people on the ground seeking to apply pressure for reform. Disgracefully, the U.K.'s current libel laws make it almost impossible to embark upon investigative journalism in relation to corruption, for fear of being bankrupted by legal action.

Whatever the merits of any individual case, the London courts have been resorted to repeatedly against U.K. journalists who have made accusations related to Russian corruption—including a suit brought against *The Economist* and settled in 2009 for an article suggesting that Gennady Timchenko had benefitted financially from his close relationship with Vladimir Putin.¹⁰² In a more recent example, Major Pavel Karpov hired P.H.A. Media to rehabilitate his reputation, while Andrew Caldecott QC and the corporate solicitors' firm Olswang have been instructed in Karpov's libel suit against Browder (a curiously high outlay for someone whose official salary is around £300 per month).¹⁰³ As Nick Cohen has argued, the use of the U.K. courts calls attention to the illiberal nature of the U.K.'s libel laws, and its abuse by wealthy "libel tourists" to prevent public scrutiny of their activities.¹⁰⁴

A U.K. VERSION OF THE "SERGEI MAGNITSKY RULE OF LAW ACCOUNTABILITY ACT"

The Sergei Magnitsky case has emerged as a symbol of the confluence of corruption and human rights in Russia—demonstrating the way in which these two malignant phenomena are linked in practice, and how they can be linked effectively as a source of leverage by external actors.

The U.K. government's reaction to demands for action on the Magnitsky case have thus far been limited to indications that certain individuals implicated in the case have been banned from entering the U.K.; but they will not be named by the Home Office. According to Dominic Raab MP, the government's response thus far has been slow. "I've been asking the authorities for an indication of who, on the list of the sixty officials named by Senators Benjamin Cardin and John McCain [co-sponsors of the U.S. "Magnitsky Act"], has been barred from entering the country, but officials say it is not policy to disclose the subjects of visa bans. It's extraordinary when you consider the public scrutiny of deportation and extradition cases. In the twenty-first century the British public should be told who we are letting in and out of the country in cases like this."¹⁰⁵

The “Magnitsky Act” is relevant to the U.K. on several fronts: first of all, the significant leverage that the U.K. has over Russia, given its status as a preferred destination for Russian money; and secondly, given the direct ties between the U.K. and the Magnitsky case itself. (This includes the British citizenship of Hermitage C.E.O. Bill Browder, who has received death threats as a result of his leadership of the Magnitsky campaign, not to mention the still-unsolved death of Alexander Perepilichny in Surrey).

The government’s narrow approach—whilst useful inasmuch as it presents an impediment to Magnitsky’s persecutors—stops short of creating a precedent and a deterrent for other corrupt officials who may be tied to abuses. Moreover, the “naming and shaming” aspect of the U.S. “Magnitsky Act” is arguably one of the most powerful tools in pressuring governments complicit in this type of behavior. “Previously the West has tried to use democracy-promotion to help Russian society, but that model hardly could be applied to Russia now with the N.G.O.s being kicked out, and with the Kremlin trying to close Russia off from foreign influence,” observed Lilia Shevtsova. “But the ‘Magnitsky Act’ allows us to create a new model of influence, this time to influence the Russian elite outside Russia—that is, the Russian elite personally integrated into the Western society.”¹⁰⁶

The British government would do well to adopt a more rigorous approach, and distance itself from accusations of softness towards the Russian government, nurtured by the Conservative Party’s alliance with United Russia in the European Democrat Group within the Parliamentary Assembly of Europe. “We can see how the U.K. has become the beneficiary of corrupt money from Russia—in real estate, in the attorneys who benefit and make the U.K. a haven for this money,” commented Vladimir Ashurkov. Ashurkov further remarked upon the links between Conservative politicians and the lobby group, Conservative Friends of Russia (now rebranded the Westminster Russia Forum following the resignation of several key supporters, including Sir Malcolm Rifkind and Robert Buckland MP, over the alleged links between the group and officials within the Russian Embassy).¹⁰⁷

Dmitry Medvedev has asserted that business leaders aren’t concerned with the Magnitsky case, maintaining it is only of interest to “[...] certain individuals who are earning political capital from it.”¹⁰⁸ Yet the appalling treatment of Magnitsky, the impunity of the perpetrators of his imprisonment and death, and the lawlessness it has revealed encapsulate the elements of most concern to businesses dealing with the Russian Federation. Medvedev’s blithe assertions to the contrary are belied by the strenuous lobbying effort

undertaken by the Russian government to prevent the passage of the “Magnitsky Act.”

Western democracies in general are increasingly at a point where they can exert influence over the Russian Federation regarding these issues, given the Russian government’s desire to boost foreign investment. The U.K. can exercise further leverage thanks to its significant position as a financial centre and a desired location for wealthy Russians to purchase assets; send their children to school; and, in some cases, establish a full- or part-time base. One of the retaliatory measures taken against the United States in response to its passage of the “Magnitsky Act” gives some indication of what the U.K. might expect by way of response. Banning U.S. citizens implicated in human-rights abuses was unintentionally funny—with a spoof video on Dozhd T.V. depicting a fake American Congressman wailing: “Absolutely all my savings are frozen in Russian banks, and I don’t know how I can go on living.”¹⁰⁹

Some observers, including Ivan Nineko of Transparency International, have suggested that the new law banning officials from holding foreign assets may be designed to neuter the effects of the “Magnitsky Act.”¹¹⁰ However, the success of such a strategy relies upon the state’s ability and willingness to enforce the new law, and, given the lack of reliable protections for property in Russia, officials are likely to continue to find ways to hide their assets abroad.

Of course, in the midst of a triple-dip recession, it is natural that politicians are loath to turn away any new source of investment or tax revenue. Yet whatever the status of bilateral relations, the U.K. will continue to be an attractive location for the entrepreneurial Russians who seek better opportunities and the protections of a free society—precisely the individuals that corruption has driven out of the country. “The U.K. is a very highly regarded destination for the rich and the new rich,” commented Mark Galeotti. “It’s very cosmopolitan, welcoming; you can buy a mansion and send your kids to public schools, take advantage of ridiculously easy libel laws. So on the one hand, we should encourage Russians who’ve made their money legitimately to come here to invest and to live, but we also need to be careful about the sources of the money coming into the country.”¹¹¹

Clearly, the lengthy roster of problems facing U.K. parliamentarians is a challenge to those seeking to make this proposed legislation a first-tier issue. Yet, according to Dominic Raab, there are reasons to be optimistic about the political prospects of a U.K. Magnitsky initiative: “It is gaining more

momentum in the public and parliamentary sphere. I think the government is still grappling with how to deal with Russia, which is obviously an important source of energy and co-operation on security and other matters. But we are talking about whether or not those with blood on their hands for torture and other heinous crimes are allowed to enter this country and buy up property or move their money around. We ought to draw a red line here. Foreign policy can't be totally divorced from ethics. Ultimately, Parliament should decide this issue."¹¹²

Prospects for meaningful action on the Magnitsky case from the European Union on an institutional level is more of a significant challenge, given the dependence of many of those constituent nations on Russian energy supplies, as well as the geopolitical power that Russia exercises in the region. In addition, Russia operates a powerful lobby in Europe, comprised of individuals (including journalists, public-affairs professionals, attorneys, and even former heads-of-state such as Gerhard Schroeder and Silvio Berlusconi) who benefit from promoting the interests of the Russian government. However, with the rise in shale-gas supplies in the next ten years, Europe is in a stronger position to challenge Russia on points of corruption and human rights, and should devote increased energy to ways to apply external pressure to help precipitate reform within the Russian Federation. The U.K. should co-operate with its European partners in order to secure action in relation to the Magnitsky case, even to a more limited degree—for instance, in the form of an E.U.-wide blacklist against the perpetrators of Magnitsky's imprisonment and death.

SUPPORT FOR RUSSIAN CIVIL SOCIETY

The U.K. Foreign and Commonwealth Office currently prioritises five areas in relation to its internal engagement with the Russian Federation: elections and democracy; freedom of expression; North Caucasus; rule of law; and equality and non-discrimination. These priorities appropriately highlight some of the systemic elements which must be addressed from within the Russian Federation if corruption is to be challenged effectively.

To this end, the U.K. Embassy in Russia should continue to engage on these issues in a forthright manner, and extend its outreach to civil society activists and groups advocating political reform and anti-corruption efforts within Russia. Similarly, the government should commit to high-level ministerial engagement with representatives of Russia's opposition movement, and parliamentarians—including the relevant All-Party Parliamentary

Groups—should extend invitations to members of Russia’s civil society to brief members on the internal situation within Russia. This will enable policymakers to receive a more rounded view of the circumstances within the country, and brainstorm opportunities for assistance and external pressure towards further anti-corruption efforts.

IMPROVED INTERNATIONAL CO-OPERATION ON ANTI-CORRUPTION EFFORTS

Over the past decade, international coordination on anti-corruption efforts has improved tremendously, with the “September 11” attacks and the global financial crisis demonstrating the profound interconnectedness and vulnerability of the global financial-system. International co-operation on this front is particularly important, as it enables improved co-operation in tracing the flow of corrupt money across borders, and facilitates more effective external pressure on corrupt countries.

The U.K. can assist the fight against corruption in Russia by supporting regional and international efforts to improve anti-corruption measures. In addition to pushing the issue forward on a regional level within the E.U., the U.K. can highlight Russia’s transparency obligations under its newly acquired World Trade Organisation membership, and through relevant international bodies.

In particular, the U.K. has a unique opportunity to use this year’s G8 presidency to promote strengthened anti-corruption efforts and boost international transparency measures, as David Cameron has advocated.¹¹³ The G20 Anti-Corruption Working Group also provides an opportunity for improved co-operation on corruption, bringing together the B.R.I.C.s and established countries. The U.K. should use this forum to continue to promote the Action Plan developed in 2010—including an emphasis on protecting whistle-blowers, and improving anti-corruption instruments within the U.N. and O.E.C.D. Furthermore, the U.K. should also treat Russia’s bid for O.E.C.D. membership as an opportunity to stress the need for increased scrutiny of meaningful actions taken towards improving the corruption landscape.

In the aftermath of the crisis triggered by a lack of responsibility and transparency within the banking sector, there is a particularly strong impetus for the international community to co-operate in promoting a rules-based financial sector; the U.K. should be at the forefront of this argument on an international level.

CONCLUSION: CORRUPTION AND RUSSIA'S FUTURE

In February 2013, photographer Misha Friedman released a series of powerful photographs entitled “Photo51—Is Corruption in Russia’s D.N.A.?” The photographs capture the visible consequences of corruption in the everyday lives of Russian citizens—from the traffic policemen collecting bribes to the major roads closed on a daily basis to allow dignitaries to drive through unimpeded by ordinary citizens.¹¹⁴ The photos underscore the way in which corruption is not only an economic problem, but a moral one, creating a society built on dishonesty and greed rather than transparency and dignity. While corruption is common to all countries, even democratic ones, it is clear that authoritarianism is both a product and enabler of corruption.

These arresting photographs beg the question of why such a corrosive phenomenon should be accepted as inevitable, both by Russians and the international community. Of course, the international community and individual states cannot, and should not, attempt to change Russia—that can only be done by the Russian people— it can stand in solidarity with the Russian people against a rapacious elite which has institutionalised theft, disrespected individual rights, and undermined the country’s future in the name of greed.

The U.K. can play a significant role in bolstering this effort to make Russia change from within, by undertaking the following measures:

- Strengthening domestic responses to the exportation of corruption via the purchase of U.K. assets with dirty funds and the use of the U.K. banking system;
- Undertaking parliamentary measures which increase transparency in relation to corruption, including libel reform and support for

the activities of Russia's anti-corruption and democratic-reform advocates;

- Passing a U.K. version of the landmark "Sergei Magnitsky Rule of Law Accountability Act"; and
- Using international platforms such as the G8 presidency to stress the global importance of improved transparency and the systemic reforms needed to tackle endemic corruption.

Now, more than ever, the U.K. has an interest and a responsibility to support the efforts to hold the Russian state to account for the malignant consequences of its fusion of political and economic corruption, consequences that affect both the Russian people and the wider world.

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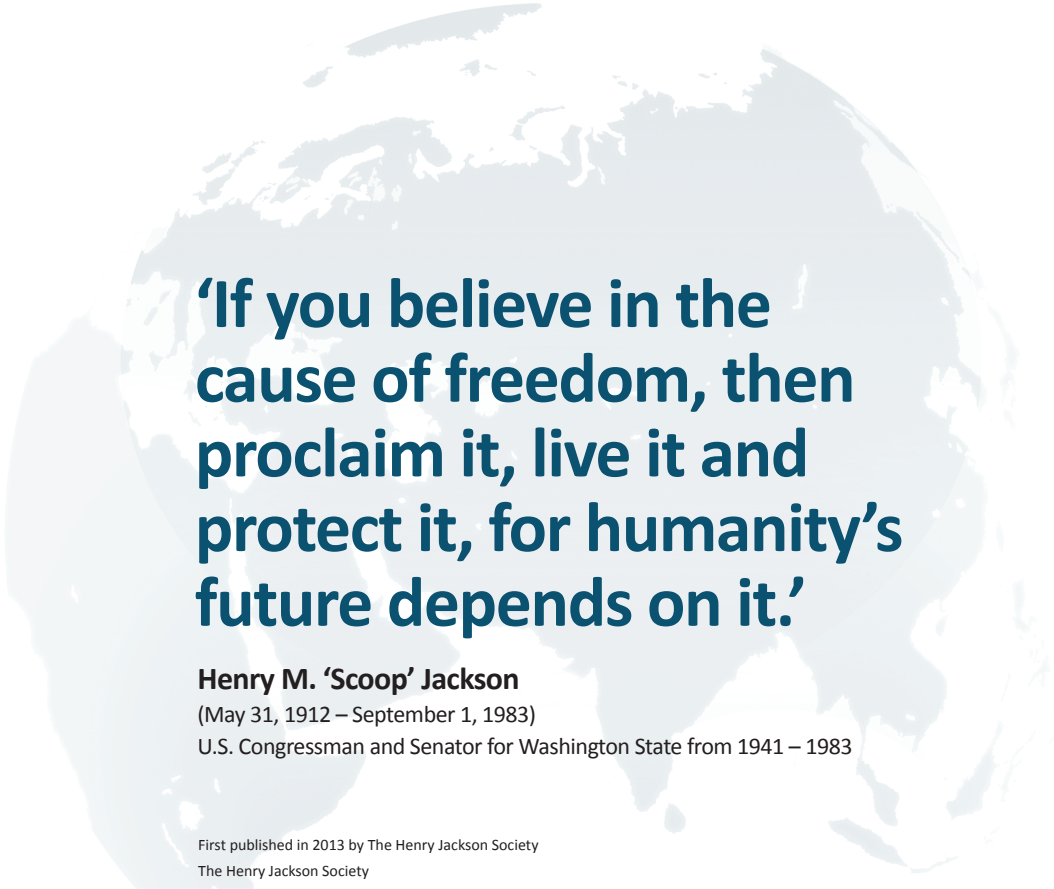
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Henry M. ‘Scoop’ Jackson

(May 31, 1912 – September 1, 1983)

U.S. Congressman and Senator for Washington State from 1941 – 1983

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