Summary and analysis of the
"Statement on the Form of the Indictment Presented to Platon Lebedev"
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After the arrest of Mikhail Khodorkovsky, then Chairman of Yukos, Russia's largest oil company last October, I distributed a summary and analysis of the charges against him as set forth in Report published by the Prosecutor General. This earlier summary and analysis was distributed on December 11, 2003 (JRL #7462) and is archived at the site: http://www.cdi.org/russia/johnson/7462-9.cfm.

As I noted in that summary, the case against Khodorkovsky has become a major focus of attention of the legal community and is being viewed as an important, if informal, precedent regarding important aspects of criminal and commercial law in Russia. Although the Western press has focused on the case as a political rather than legal event, considerable attention is being devoted in Russia to the case itself, how it is being conducted and what it means for doing business here.

In my previous comments I stated that it was important for the legal community to keep an eye on this case both to understand its implications and also to raise any issues regarding how it is being prosecuted. Therefore, with the publication by the Prosecutor General's office, on April 1, 2004, of a "Statement" setting forth the charges against Khodorkovsky's business partner, Platon Lebedev, I am providing here a similar review of this Statement. Below, I will briefly review the difference between the charges and allegation made against Lebedev in the Statement and those made against Khodorkovsky in the Report. Then I will comment on some of the more general aspects of the case and related proceedings that have been reported on in the press.

A rough translation of the Statement is being prepared by my office, which will make available to those who request it at pclateman@spkgroup.com.

I. Summary and Analysis of the Statement

For brevity, I will refer to Lebedev as "L" and Khodorkovsky as "K" in the summary below.

A. General observations

Of the ten criminal charges made against L in the Statement and the eleven made against K in the Report, nine overlap and appear to be based upon the same set of facts. Given the large overlap, I focus on the differences between the charges in my comments below.

Overall, the Statement provides an additional level of detail not found in the Report regarding the connections between members of the alleged "organized group" that carried out the various crimes. (I refer to my previous comments for more discussion regarding "organized groups" under Russian law and their relation to the charges in the indictment.) A short introductory section summarizes the main characters in the group and their official titles and connections. In addition to K and L, A.B. Krainov, a department head at MFO "Menatep" is mentioned as a leading figure. He is accused of appointing and then directing the actions of the general directors of various companies used in the schemes. N.V. Chenishev, head of the privatization department of Bank Menatep, is also identified

as a leading figure. It is alleged that he directed other bank employees regarding the preparation of documents for the companies that participated in the Apatit privatization (among other supervisory activities). V.V. Moyseev is also named as a key figure in many of the charges, usually acting as the Russian representative of foreign entities which participated the alleged schemes. He was apparently an assistant to K while K served as the Chairman of the Board of MFO "Menatep". Moyseev is also described as a "trusted" childhood school friend of K. More than a dozen other persons connected with Menatep are named as playing dual-roles within Menatep companies and, simultaneously, within the companies involved in the alleged crimes. The naming of these individuals may indicate that charges will be brought against some of them as well.

Although the concept of "organized group" bears certain similarities with the concepts of "organized crime" as defined in organized crimes statutes in the US, the analogy is only partial. An "organized group" under Russian law is closer to a group of accomplices under US law. It does not require the use of a legal entity or of a quasi-corporate entity. Forming and acting as an "organized group" does not form a separate crime (although it stiffens the punishment applicable to specific crimes). The Russian Criminal Code does contain a separate concept of "organized crime"--Article 210 of the Criminal Code establishes a separate crime for what more specifically mirrors the definition of "organized crime" under US federal and local statutes. However, neither Khodorkovsky nor Lebedev are charged with violating this article. I speculate below (in discussion of the potential for a jury trial) why the prosecutors may have refrained from making this charge.

It should be noted that since the Report was published, the Russian Criminal Code and the Criminal Procedural Code have undergone major revisions, which were adopted on December 8, 2003 (some provisions of which come into force only on May 12, 2004). The revisions to the Criminal Code do not appear to have changed the substance of any of the charges made in the current case (although reorganization of some of the articles of the Criminal Code has resulted in changes to the paragraph numbering cited in some of the charges.) Although I have not reviewed the punishments applicable to the crimes charged, I note that the punishments applicable to certain crimes included in the indictment are affected by the amendments.

B. Summary and analysis of the charges

1. <u>Fraud on a large scale committed through the use of an organized group by obtaining rights to another's property by deceit (part 4, Article 159 of the Criminal Code)</u>.

This is the same fraud charge that has been made against K in the Report in connection with the failure to fulfill the investment conditions under the privatization of a 20% stake of the fertilizer company "Apatit". (See charge "1" in my previous summary.)

2. <u>Willful violation of an effective court order by an employee of a commercial organization (part 3, Article 33 and Article 315 of the Criminal Code of the Russian Federation)</u>

This is the same charge of violating a court order that has been made against K in the Report in connection with the failure of K and L to secure the return of the shares of Apatit as ordered by the Moscow Arbitration court after the privatization of the Apatit shares had been annulled. (See charge "2" in my previous summary.)

Although the charge is the same, I note that additional factual allegations have been added that make the nature of the violation of the court order clearer:

In the Report, the prosecutor alleged that K and L violated a court order issued in 1999 by the Moscow Arbitration Court against Volna, the company allegedly controlled by K and L which won the Apatit privatization tender, but allegedly failed to make the $283 million investment it promised. The court ordered Volna to return the Apatit shares to the State Property Fund. It is alleged that K and L had the power to cause the shares to be returned because they had caused them to be moved under sham transactions to other companies also under their control. I noted in my comments to the Report that such a failure to take positive measures to comply with the order could be interpreted as a criminal violation of the order, but a rather abstract one that could be subject to challenge by the defense. In the Statement, however, the prosecutor has added allegations that K and L took steps to move the Apatit shares to a further set of companies even after the court order was issued for the purpose of further hiding them from the authorities. Allegations of such active steps to thwart fulfillment of the court order more clearly constitute a criminal act and correct a potential weakness in the prosecutor's position with respect to this charge.

3. Causing large-scale economic harm to the owner of property through deceit other than by embezzlement (points a, part 3, Article 165 of the Criminal Code of the Russian Federation)

This is the same charge of causing economic harm that has been made against K in the Report in connection with the scheme by which K and L allegedly caused Apatit to sell its products at below market prices to companies controlled by K and L. These "fictitious" companies then allegedly resold the products at market prices, depriving Apatit and its shareholders of some RUR 6.1 billion (approximately $200 million) of profit that would otherwise have accrued to them during the period 2000-2002. (See charge "3" in my previous summary.)

I note that, in my earlier analysis, I incorrectly referred to this charge as "embezzlement". If fact, the crime charged is "waste" or "economic harm". The difference between these charges is that proving "economic harm" does not require proving that the defendant benefited from the harm caused to the victim. "Embezzlement" requires a showing that the defendant somehow took property or rights away from the victim through the scheme. Although the prosecutor does allege that K and L converted the profits from this scheme to their own use, it is possible that prosecutor cannot substantiate this claim. For this or some other reason, only the lesser charge of "economic harm" has been applied to this scheme.

The analogous charge against K in the Report is slightly different from the charge made here: L is charged only under point "a" of part 3 of Article 165 of the Criminal Code (causing economic harm through an organized group), but not under point "b" of this part (causing such harm in a "particularly large amount"). K is charged under both points "a" and "b". Given that K and L are charged under the same set of allegations, it is unclear why point "b" is omitted in the charge against L.

4. Embezzlement of another's property, entrusted to the accused, through the use of his official capacities, in a large-scale and committed through an organized group (part 4, Article 160 of the Criminal Code).

This is a new charge: K and L are accused of leading an organized group in the embezzlement of $32.5 million from Apatit in connection with a transfer pricing scheme. Although this charge is based on the same scheme described in the previous charge, it focuses on a different set of transactions which took place during 1997-2000. Specific allegations made regarding these transactions and the flow of funds serve to demonstrate that K and L, through the organized group, converted funds representing the transfer price difference to their own use. This charge is straightforward embezzlement.

The reason for this charge (in which K is also implicated) appearing now and not in the earlier indictment against K is possibly due new discoveries by the prosecutor in the course of further investigation. Therefore, it is possible that this charge will be added to the indictment against K as well. It is also possible that this charge has already been brought against K, but that it has not yet been made public.

5. Fraud on a large scale committed through use of an organized group by obtaining rights to another's property through deceit (part 4 of Section 159 of the Criminal Code)

This is the same charge of fraud that has been made against K in the Report in relation to the privatization of 44% of the shares of the Joint Stock Company "Scientific Research Institute for Fertilizer and Insecto-Fungicides in the name of Professor Ya. V. Samoilev" (abbreviated in Russian as "NIUIF"). (See charge "4" in my previous summary.)

6. Willful violation of an effective court order by an employee of a commercial organization (part 3, article 33 and article 315 of the Criminal Code of the Russian Federation)

This is the same charge of violating a court order that has been made against K in the Report in connection with the failure of K and L to secure the return of the shares of NIUIF as ordered by the Moscow Arbitration court after the privatization of NIUIF shares had been annulled. (See charge "5" in my previous summary.)

7. Large-scale tax evasion carried out through an organized group (part 3 of Article 33 and points a, b, part 2 of Article 199 of the Criminal Code)

This is the same charge of tax evasion (filing a false tax return) that has been made against K in the Report in connection with a scheme carried out by Yukos affiliates to pay taxes using promissory notes (instead of cash) in violation of the Tax Code. The amount of unpaid tax is stated to be RUR 5.4 billion. (See charge "6" of my previous summary.)

As I stated in my previous summary, one of the defects in the pleading of this charge is that the prosecutor fails to allege specifically which tax return the charge is referring to and what information in the return was false.

In the Statement, the prosecutor attempts to remedy this defect: the prosecutor now alleges that each of the Yukos affiliates that allegedly took part in this scheme (the Russian limited liability companies "Mitra", "Business-Oil", "Vald-Oil" and "Forest Oil") improperly indicated that it owed no tax on its annual accounting statement for 1999 (the year in which such payments allegedly occurred) (in particular, in box 4 of line 626 of their respective balance sheets in the form required

by Attachment No. 1 to the Regulation on Accounting Records No. 4/96, confirmed by Ministry of Finance Decree No. 10, dated February 8, 1996). The submission of such a balance sheet to the tax inspectorate is mandatory pursuant to subparagraph 4, point 1 of Article 23 of the Tax Code. The company reported in this box on its balance sheet that it owed no tax, which was a false filing because it had not in fact paid tax (since it had paid improperly with promissory notes).

In my view, this additional allegation corrects one of the pleading defects, which I pointed out in my previous comments. However, I refer readers to my previous comments regarding additional potential defects in this charge that have not been corrected.

8. Exceptionally large-scale evasion of corporate tax carried out through an organized group (part 3 of Article 33 and paragraphs a and b, part 2 of Article 199 of the Criminal Code)

This is the same charge of tax evasion (filing a false tax return) that has been made against K in the Report in connection with a tax scheme involving the same companies referred to in the previous charge. K and L are charged with causing these companies to evade taxes in the year 2000 through three schemes: (i) paying taxes in promissory notes (the same scheme described in the previous charge); (ii) improperly claiming a tax concession granted to companies operating in low tax zone within Russia (referred to as "ZATOs"); and (iii) improperly "overpaying" taxes with promissory notes and then illegally claiming an offset of such "overpayment" against taxes due in the next accounting period. (See charge "7" of my previous summary.)

With respect to this charge, as is the case with charge "7" above, the Statement adds specific references to tax returns that were filed containing false information. The Report did not contain such specific references with respect to bases (i) and (ii) for this charge. Therefore, in my comments to the Report, I had noted that this absence was a defect in the charge with respect to bases (i) and (ii).

With respect to basis (i) (payment of taxes with promissory notes), the defect in the charge seems to me to have been corrected by an new reference to the filing of a corporate balance sheet containing a false assertion that no taxes were due. This is the same correction that was made with respect to charge "7" above. Despite this correction, the pleading of this charge continues to suffer from the other defects I pointed out in my previous comments.

With respect to basis (ii) (improperly claiming the ZATO tax concession), references to a particular tax form on which the tax concession was improperly claimed are not sufficient to correct the defect I discussed in my comments to the Report. In the Report, and again in the Statement, the prosecutor simply asserts that the company in question (Business Oil) was not entitled to the ZATO tax concession because it had no actual activity in the region. The question of whether Business Oil included false information in its tax return by claiming the benefit of this concession is properly called a "mixed question of fact and law". That is, to support this assertion we must look both to the laws entitling companies to claim the concession and then analyze the facts to determine whether such rules were violated. Under the general legislation on ZATOs, it appears to have been within the regional authority's power to grant the concession to companies in the region without reference to whether the main activities of the company were in fact within the region. There may be unpublished local acts to which I do no have access, but the prosecutor neither alleges that (i) Business Oil had not been granted the concession nor (ii) if it had been granted, it was granted in violation of a particular rule. In other words, the assertions made are insufficient to substantiate the

legal conclusion that Business Oil did not have the right to the concession and that, in turn, the tax return was false.

The prosecutor's attempt to construct a charge of criminal tax evasion out of improper use of the ZATO tax concession has been greeted with considerable skepticism in the Russian press and among many of my Russian colleagues. As I noted in my earlier comments, the abuse of the ZATO regime was widely reported in the press and commented upon over a number of years and resulted in amendments to the relevant legislation to close the apparent loophole. Nevertheless, I have heard discussion of a number of alternate theories under which such use of the ZATO tax concession could be challenged. The soundest theory that I have heard is that the use of the concession may be challenged by attacking the agreements between the real production companies and the shell companies in the ZATO. As in the price transfer scheme described in charges 3 and 4 above, these agreements may be challenged as "fictitious" because they were not concluded on an arm's length basis. The production companies transferred their products to the intermediary companies in the ZATO at below market rate for the sole purpose of transferring revenue to them to take advantage of tax concession and/or embezzling money from them. If such agreements are fictitious, then the revenue and profit from such agreements should be attributed to the production companies. This would provide a mechanism for the tax authorities to recover the underpayment of tax. Of course, adopting this theory or another new theory as the basis of this charge would constitute a major amendment to the indictment.

9. Large-scale fraud committed through use of an organized group by obtaining rights to another's property through deceit (part 4 of Section 159 of the Criminal Code)

This is the same charge of fraud that has been made against K in the Report in connection with a tax scheme by which K and L illegally caused the same companies referred to in the previous charge to overpay their taxes "illegally" with promissory notes and then file for and receive cash refunds from the budget. (See charge "8" of my previous summary.)

10. Large-scale tax evasion by a physical person through knowingly providing false information in tax filing (part 2, Section 198 of the Criminal Code)

L is charged with illegally using the tax regime applicable to "individual entrepreneurs" to receive as "consulting fees" and pay reduced tax, despite the fact that such compensation was actually for his employment as an officer of Bank Menatep, Rosprom and Yukos-Moskva. K and is charged with using the scheme to reduce his personal income taxes. (See charge "10" of my previous summary.)

I note that in the Statement, the prosecutor claims that other senior employees of these companies used the same illegal tax evasion scheme. It is therefore possible that these individuals may face prosecution as well.

C. Missing Charges

Two charges made against K have not been repeated against L:

In charge "9" of the Report, K and L, through the actions of the organized group, allegedly embezzled funds from Yukos and its affiliates by selling apparently worthless promissory notes to such companies for cash and transferring the funds companies related to Vladimir Gusinsky. One

can only guess why this charge has not been repeated against L, despite the fact that the Report alleges that he was a leader of the group that carried out this scheme. As I noted in my earlier comments, the factual allegations made in relation to this charge in the Report are incredibly sparse. It is possible that the prosecutor simply lacks evidence to substantiate this charge. If so, the charge may have been withdrawn from the indictment against K as well. On the other hand, the charge may be added later after completion of further investigation.

In charge "11" of the Report, K is charged with "forging" documents submitted to the tax authorities in connection with the scheme to avoid personal income tax (this scheme is the basis of charge "10" above and charge "10" in the Report). As I noted in my comments to the Report, the prosecutor's application of Article 327 of the Criminal Code (forgery) did not fit the facts as K was not accused of falsifying documents, but rather filing documents containing false information. Although the Statement makes the same factual allegation against L, the prosecutor has not charged L with violating Article 327. Perhaps the prosecutor has reconsidered his interpretation of Article 327 and will drop this charge against K as well.

II. Additional Observations on the Proceedings

A. Pre-Trial Detention

1. The question of "bail"

Much comment in the press has been devoted to the length and nature of the pre-trial detention of Khodorkovsky and Lebedev. The main issue that has been raised in the press is that neither Khodorkovsky nor Lebedev have been granted "bail" or otherwise released from prison while awaiting trial. Under the current Criminal Procedure Code, the factors to consider in releasing the accused pre-trial are similar to the factors that apply in other countries: the risks that the accused might continue to conduct criminal activity; might take measure to interfere with an ongoing investigation or with witnesses; or might flee the jurisdiction or elude investigators. The judge has wide discretion to determine which facts regarding the defendant are relevant to assessing these risks, including the apparent strength of the indictment itself. Although I have not seen specific data, I venture to say that the release of defendants pre-trial (with or without posting of bail) is much less common in the case of serious crimes in Russia than in the US or the UK. Therefore, the failure to release Khodorkovsky and Lebedev in the Russian context is not surprising.

Although I have not had access to the arguments put forth in the hearing on this matter, it can nevertheless be ventured that these defendants in such a case would not be released pre-trial in the US or the UK either. Firstly, the indictments appear strong with respect to a number of serious charges. A number of the crimes allegedly involve repeated acts of dishonesty and fraud. A significant portion (if not the bulk) of the defendants' assets are located abroad. They own airplanes and employ numerous security and support personnel who could facilitate their flight. They are accused of crimes that involved operating a network of trusted individuals, many of whom are still under investigation but have not been arrested and could easily be tampered with. The fact that a number of their partners in the alleged crimes (including those charged and uncharged) have, in fact, fled the country must also be seen as a highly relevant consideration. In response, the defendants could cite the lack of previous convictions, their reputation and standing in the community and desire to maintain it, the interest of their families and the businesses they own. However, it seems to me the balance tilts against them.

2. Length of detention/speedy trial

Questions regarding the length of the pre-trial detention have been raised in the press by representatives of the accused and others. However, some of the concerns raised are contradictory. On the one hand, the defendants are entitled to a speedy trail. On the other hand, the defendants must be given time to prepare their defense. It appears that, at least with respect to the case against Lebedev, what would be considered in most countries "speedy trial" will occur (the trial is expected to begin in a matter of days, some nine months after his arrest). According to press reports, the case against Khodorkovsky is also proceeding quickly. Therefore, it appears to be a greater concern that the defendants' rights are being violated by the rapid schedule set by the prosecutor and court which may not allow time to prepare a defense. Some reports have contained complaints by the defendants' representatives about the volume and complicated nature of the evidence turned over by the prosecutor and the short time given to the defendants to prepare. There is simply no information available on which to venture a guess as to whether enough time is being given to the defense. (Recent reports indicate that Lebedev's representatives have been focusing on obtaining a speedy trial and not complaining about the rapid scheduling of the hearing.) In any event, given that these trials are proceeding quickly (for trials of their kind) by both Russian and international standards, the denial of any request by the defendants for an extension would raise serious questions about due process and whether the timing of the trials is being controlled to hamper the defense or for other (i.e., political) reasons.

It should be mentioned that lengthy pre-trial detention is in fact a big problem in Russia. The cozy relation between judges and prosecutors often results in arrest warrants being issued against suspects on very poorly pleaded indictments. After the arrest of an accused, the prosecutor continues a leisurely investigation and slowly amends defects in the pleading, often changing the entire theory of the case and lodging entirely new charges while the accused languishes in prison. Judges liberally permit amendments to indictments or even permit the investigation against the defendant to be reopened, while refusing requests to bring the existing charges to trial. In Western jurisdictions, judges are far stricter in reviewing requests to amend indictments and a prisoner will typically be released if the prosecutor attempts to make major amendments to the charges after arrest or even the start of trial. Although it does not appear that such machinations have taken place in the current case so far, it is possible that, if the prosecutor faces setback at trial, we may see attempts by the prosecutor to amend the charges or reopen the investigation, in which case the question of whether the defendants are being denied a speedy trial will come back to the forefront.

3. Conditions of pre-trial detention

The conditions of the pre-trail detention of Khodorkovsky and, particularly, Lebedev have been another focus of protest. Lebedev's attorneys have claimed that he is being denied necessary medical attention. Alexei Pichugin, the former head of Yukos's security department, who has been accused of murder, claims that he was drugged while in custody by FSB officers. Some reports have noted that a judge refused to grant Lebedev a magnifying glass to read documents in prison (although it smacks of sensationalism for Lebedev's lawyers to have made such a request to a judge in a proceeding unrelated to such details of his detention). It has been reported that a claim was in fact filed on Khodorkovsky's and Lebedev's behalf in the European Court of Human Rights regarding the conditions of their detention. According to some reports, the refusal to release Khodorkovsky on bail is one aspect of the claim that has been filed (but as I have stated above, it does not seem that this detention is unreasonable in principle). Regardless of how these claims of mistreatment are sorted out (and they are certainly disturbing even if unfortunately all too typical of

the Russian criminal justice system) they do not appear to be related to the procedural or substantive aspects of the cases themselves. Khodorkovsky's lawyers have publicly declared Khodorkovsky to be a "political prisoner". Therefore it is likely that Khodorkovsky and Lebedev will file a human rights complaint based on the substance and procedure of the case and the trial, but only once these processes have developed further.

B. Publication of the Charges

Khodorkovsky's and Lebedev's representatives have complained about the publication of the Report and the Statement. In some articles, the complaint appears to be directed at the publication of these documents themselves. In other instances, they complain about the publication of the charges at a time when the defendants are under court order not to reveal other documents related to the prosecutor's case that have been revealed to them in confidence.

Of course, the more common complaint about the Russian criminal justice system in this area is that charges are often *not* revealed publicly, even after the trial starts. All too often, thin connections with national security or the need to protect ongoing investigations are given as pretexts for thwarting the fundamental right to a public trial and transparency of the process in general. Having reviewed the relevant provisions of the Criminal Procedure Code, I see no violation of Russian law in the timing of the publication of the charges. Nor do I see anything unusual with the prosecutor publishing these charges while at the same time requiring the defense to keep confidential certain materials that the prosecutor has handed over to the defense. Roughly the same sequence of events is common in the US. Moreover, we are all familiar with the extremely public grandstanding, "spin control" and other forms of far less neutral public relations methods employed by US prosecutors in the pre-trial phase, including extensive and repeated interviews and news conferences with prosecutors in which charges are often discussed (although particular evidence is not discussed). At some point, such methods may rise to a violation of due process, but it is hard to see how the mere publication of the charges could be such a violation.

C. Jury Trial

According to press reports, L has requested a trial by jury. Under the current Criminal Procedure Code (which implements the Constitutional right to trial by jury), there do not appear to be any grounds on which to review such a request. Jury trials are granted as a matter of right under the Criminal Procedure Code when charges (specified in Article 31 of the Criminal Procedure Code) have been made. In the indictments against Khodorkovsky and Lebedev, no applicable charges have been made. Therefore, it is quite difficult to see on what bases Lebedev's request for a jury trial could be entertained. More likely, the response will simply be that there is no basis to make such a request.

On the one hand, the prosecution of K and L is reportedly supported in the polls. On the other hand, in the US experience, prosecutors have a harder time winning convictions in jury trials in complicated financial fraud cases. A jury trial is more complicated procedurally, which increases the chances of errors and the possibility for a mistrial and appeals (recent US examples include the cases against Frank Quattrone and Denis Kozlowsky).

As noted in the general comments above, the prosecutor has not charged Khodorkovsky and Lebedev with "organized crime" although the facts alleged in the indictments would support such a charge. If this charge had been made, it would have triggered an automatic right to a jury trial under

the Criminal Procedure Code. We may speculate that Lebedev has requested a jury trial on the basis that the factual allegations made against him constitute "organized crime" and therefore he should be entitled to a jury trial even if the prosecutor has avoided making this charge. I refrain from attempting to analyze this argument until it is clear that it has been put forward.

D. Arrest, Seizure and Confiscation of Assets

Since the arrest of Lebedev last June, there has been widespread speculation that the ultimate goal of this prosecution is the confiscation and redistribution of the wealth of Khodorkovsky, Lebedev and their associates. As I explain below, the prosecutor, the government and other interested parties have absolutely no legal basis (based on the charges brought so far and the facts alleged in the Report and the Statement) to receive as compensation or otherwise seize more than small portion of the wealth of these individuals.

Undoubtedly fueled by this speculation about the motives behind the prosecution, a number of articles have incorrectly stated that assets belonging to Menatep and/or its "core shareholders" have been "seized" or "confiscated". It is quite clear from reviewing the details of such reports that there has not yet been any "seizure" or "confiscation" of assets. What has apparently occurred is that certain assets allegedly belonging to Khodorkovsky, Lebedev and their associates have been frozen as security to satisfy various claims that have been or might be made against them. As I explain below, these claims are limited and cannot result in a general confiscation of the defendants' wealth.

1. Confiscation

A number of recent Russian and foreign articles on the case continue to play up the theory that some or all of the assets of Khodorkovsky, Lebedev and their associates will be "confiscated" simply by virtue of their conviction of a serious "felony" under the Criminal Code. The history of "confiscation" under the Russian Criminal Code over the past decade would make an interesting digression—but the current status of this history is that such confiscation has been entirely removed from the Criminal Code with the amendments adopted on December 8, 2003. (President Putin of course signed the new draft of the Criminal Code and it is generally reported that the Presidential Administration has been the driving force behind completing amendments to the Criminal Code.)

The removal from the Criminal Code of what were draconian confiscation provisions was only partially applauded by those monitoring the development of the legal system in Russia. While the provisions that were removed resembled outmoded rules that disappeared in Europe in the 19th century and in the US with the Bill of Rights, most western countries have in fact reintroduced some form of confiscation of property in relation to crimes that have an economic nature or goal, providing that the property can be shown to be the fruit of the crime. Put simply, the US and many European countries have concluded in the past few decades that the concept that "crime should not pay" is not always at odds with due process. However, at present, there is simply no mechanism in Russia for the prosecutor or state to confiscate the assets of Khodorkovsky, Lebedev or their associates simply by virtue of convicting them of a crime. Even if the Russian Criminal Code is further amended to include modern confiscation provisions, they could not be applied to this case, as the Constitution prohibits the retroactive application of amendments to the Criminal Code that worsen the position of a defendant. Of course, the removal of the confiscation provisions from the Criminal Code has much wider implications—clearly, by introducing such a change, the "powers that be" have eliminated a vital tool for the redistribution of property, which would seem to question the widespread concern redistribution of property is in fact their intended goal.

2. Other claims and freezing orders

Despite the fact that no "confiscation" may take place, based on the criminal charges made against the "organized group", it is not difficult to contemplate that there are a number of interested parties (for example, the State Property Fund and the tax authorities, among others) that have been damaged by the alleged fraud, tax evasion and embezzlement schemes alleged in the Report and the Statement. These parties would have claims to recovery money and assets from the defendants. Neither the Report nor the Statement contains any specific claims for monetary damages which necessarily form the basis for obtaining a freezing or similar court order, but it is clear how such claims would be formulated on the basis of those charges and the facts alleged. In Russia, as in other civil law countries, the prosecutor may defend the interests of the affected parties by seeking to freeze the assets of the defendants to secure against a future monetary judgment. The freezing of assets is not a seizure or a confiscation, but merely prevents the defendants from disposing of the assets before the claims of the affected parties are resolved and they receive any compensation to which they might be due.

Therefore, it is not surprising that freezing orders have been sought or that they have been granted in the context of the current prosecution. Unfortunately, without actually seeing the court orders and the court submissions on which they are based, it is not possible to provide much meaningful comment (or criticism) of such orders. (I would be glad to receive them from anyone who has obtained them from public sources at pclateman@spkgroup.com.) Nevertheless, it is possible to venture some broad observations.

By reading the charges in the Report and the Statement, it is possible to estimate the aggregate amount of damages (including unpaid tax) that could be sought through claims brought under the criminal charges. In a number of places in the charges, the sums of money indicating the amount of tax illegally avoided and the damages caused by the charges of fraud and embezzlement do not clearly add up. Even if we take the maximum amount of damages implied by the fuzzy arithmetic in the indictments and make certain conservative assumptions about the applicable ruble conversion rate, there does not appear to be more than $2.5-3.5 billion of damages asserted in the indictments. Furthermore, it should be kept in mind that any unpaid tax (other than the relatively miniscule amounts claimed in relation to the personal income tax evasion charges) should not be owed by Khodorkovsky and Lebedev personally, but by the various Yukos affiliates from whom such tax was due. (Khodorkovsky and Lebedev may, however, be held liable for the interest and penalties incurred by such companies as a result of having participated in these illegal schemes.) Therefore, it is possible that the maximum figure of recoverable damages against Khodorkovsky and Lebedev personally in connection with these charges is considerably lower than $2-3 billion.

According to press reports, the bulk of the Yukos shares allegedly owned by the leading members of the "organized group" have been frozen (this block is reportedly valued at roughly $15 billion). An additional $5 billion of cash held in foreign accounts has also been frozen. The value of these assets far exceeds the amount of damages identified by the indictments. Therefore, there are either other claims being made by the government of which we are not yet aware or we can expect Khodorkovsky's and Lebedev's lawyers to apply to reduce the scope of the freezing order to release some of the assets. (Of course they will seek to challenge the freezing orders numerous other grounds, but it is not possible to speculate on these matters without further information).

3. Fines

I note for the sake of completeness that Khodorkovsky and Lebedev are subject under the Criminal Code to being fined if convicted of the charges made. These fines would be in addition to my rough assessment of maximum damages based upon the charges and allegations made in the indictments ($2.5-3.5 billion). To estimate what the maximum amount of such fines could be based upon such charges and allegations would require much speculation because the definition of these fines is new under the December amendments to the Criminal Code and their calculation would require facts which we do not have. My own attempt at such an analysis (which I omit here) says that the fines, if imposed, cannot rise to level at which they would represent a serious element of the overall economics of the case. I hope to provide further comment if it appears that such fines become a more important element of the case.

E. "Plea bargaining" or otherwise cutting a deal

Most recent speculation regarding these cases in the press revolves around prospects for Khodorkovsky and/or Lebedev "to cut a deal" to get out of jail.

Russian law does not provide for what we in the US call "plea bargaining"—the elimination of charges from an indictment and/or the setting of a pre-agreed sentence for specific charges in exchange for a plea of guilty (in lieu of trial) and/or cooperation with the prosecution. The only form of such bargaining that it officially permitted is for the prosecutor to trade unofficial promises of support for leniency before the sentencing court in exchange for cooperation and/or a guilty plea.

Undoubtedly, in practice, there is a myriad of informal and illegal agreements entered into between prosecutors and defendants on a regular basis in Russia (from straightforward bribery to arrangements that may have a more noble intent). It is has been widely reported that a number of "oligarchs" were offered and even made trade-offs involving the transfer of asset in exchange for not brining (or dropping) criminal charges. It cannot be ruled out that such a deal could be cut in this case, but I do not believe the legal scope of "prosecutorial discretion" would permit him to cut such a deal at this stage of case. Any such deal would in fact constitute a form of corruption (or "abuse of office") by the officials involved. The exception to this is, of course, a presidential pardon.

F. Legal Ramifications

As I mentioned above and in my previous comments, a significant segment of the legal community in Moscow is following this case as an informal precedent regarding how the authorities will interpret various aspects of commercial law and the tax code. While it is a widespread view that this prosecution is "politically motivated", the implications of the prosecution's case and the handling of the trial are not being viewed as "one offs" applicable only to these defendants. I have a lot of personal anecdotal evidence that this case is changing not only how important legal concepts are understood, but how business in practiced many business groups in Moscow.

Most starkly, these indictments demonstrate that the authorities are developing greater expertise in discerning the nature of fraud and tax evasion and in prosecuting these crimes. In particular, we are seeing a more sophisticated understanding and application of three legal concepts: the inviolability of legal entities, the rights of a "good faith purchaser" and the sanctity of contract. Ironically, legal advisors and foreign investors who came to Russia over the past 15 years have never tired of emphasizing how the strength of these concepts is vital for a market economy. These concepts, however, have been adopted in Russian in a formalistic way in which the exceptions (which are

often subtle and not themselves easily applied in a formalistic manner) receive little attention. The result is that these concepts are too often abused as tools for fraud, embezzlement and tax evasion. However, the exceptions themselves can be abused—only when legal entities truly have no independent existence or have been used intentionally to defraud creditors should their inviolability be questioned; only when there is proof that a purchaser knew of a third party's claim to property or when there is good reason to impute such knowledge (such as actual affiliation) should a purchaser's rights be questioned; only where there is specific evidence that a contract is a sham meant to secrete assets or effect transfer pricing the substance of its terms be questioned. It is safe to say that the proper application of the exceptions to these principles is as important for the protection of property and functioning of the market as adoption of the principles themselves. Since this balance is so important, it is worth continuing to watch this case to monitor whether it represents a new level of sophistication in the rule of law in Russia and not just a swinging of the pendulum to a new extreme of formalism and abuse.