

Restoring Russia's Respect for the Rule of Law
Testimony of Alan Larson
before the Commission on Security and Cooperation in Europe
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Chairman Smith, Co-chairman Wicker, distinguished members of the Commission. Thank you for the opportunity to testify before the Commission on Security & Cooperation in Europe. Today we will be discussing a serious international problem, Russia's failure to respect the rule of law and the commitments it has made during the past twenty-five years.

My name is Alan Larson. I am Senior International Policy Advisor at Covington & Burling LLP. I also serve as the Chairman of the Board of Directors of Transparency International-USA, an anti-corruption NGO. Formerly I was a career Foreign Service Officer and served as Under Secretary of State for Economic Affairs during the administrations of Bill Clinton and George W. Bush. My testimony has been informed by experiences in each of these roles, but my testimony today reflects my own views and does not necessarily reflect the views of any of the organizations with which I am or have been affiliated.

The Coherence of the Helsinki Framework

The Helsinki framework is an important and creative response to the end of the Cold War. I have been privileged to play a small role in implementing parts of the international economic dimension of the Helsinki framework during the past two and a half decades. During my assignment as the U.S. Ambassador to the Organization for Economic Cooperation and Development (OECD) from 1990-1993, I helped stimulate the creation of OECD technical assistance programs for the formerly Communist countries of Poland, Hungary and Czechoslovakia. As part of this effort, the OECD developed a pathway to the accession of these countries into membership in this club of market-oriented Western democracies. Today Poland, Hungary, the Czech Republic, the Slovak Republic, Estonia, and Slovenia are OECD members.

As Under Secretary of State and Assistant Secretary of State from 1996-2004, I worked with Russian economic policy leaders on a range of international economic policy issues, including trade, debt and finance. As a member of the U.S. team in charge of preparation for meetings of G-8 Leaders, I worked closely with representatives of Russia on issues of central importance to the international agendas of President Bill Clinton and George W. Bush. These efforts were part of a broader U.S. strategy of drawing Russia and other countries of the former East Bloc into international institutions that undergird security, prosperity and individual rights.

The Helsinki framework is grounded in the realization that lasting security, meaningful economic cooperation, and respect for human rights all rest on a common foundation — strong respect for the rule of law and international agreements. A stable security system in Europe depends on collective adherence to the 10 principles guiding relations between states: beginning with sovereign equality, refraining from the use of force and the inviolability of borders

including with “the fulfillment in good faith of obligations under international law.”¹ In short, when relations between governments in Europe are governed by the rule of law and respect to international agreements, security is enhanced. When these principles are trampled on, confidence, predictability and security are eroded.

Respect for human rights is equally important to the Helsinki framework. In democratic societies, the rule of law also must govern relationships between governments and their citizens. When governments violate their own peoples’ legal and human rights, those same governments are far more likely to ignore the rule of law in their dealings with other countries and those countries’ citizens.

The economic dimension of the Helsinki framework is the dimension to which I have devoted a great portion of my career. Strong economic cooperation among states can stimulate shared benefits and constructive interdependence that, in turn, foster security and political security; at the same time, governments’ commitment to multilateral security arrangements is a necessary condition for economic cooperation to fully flower. In a similar fashion, when governments respect the rights of their people, enterprise and economic initiative flourishes; at the same time, strong economic performance can help generate resources that allow governments to fully carry out their human development obligations. The respect for the rule of law lies at the center of the relationships that make durable and meaningful economic development possible.

The three dimensions of the Helsinki framework form a coherent and interlocking whole. When all three dimensions are respected, the aspirations of the peoples of Europe for security, prosperity and freedom can be met. When one or more dimensions of the Helsinki framework are ignored, the entire framework becomes unstable.

A Closer Look at the Economic Dimension of the Helsinki Framework

I would like to focus on the economic and business dimension of the Helsinki framework. In 2012 I testified before the Senate Finance Committee on the topic of Permanent Normal Trade Relations (PNTR) between the United States and Russia. I urged Congress immediately and unconditionally to extend PNTR to Russia. I said then and I continue to believe that it was a good thing for Russia to join the World Trade Organization. By doing so and by applying rule of law disciplines to its trading relationship with the United States and other WTO members, Russia could take an important step toward meeting the terms of the Helsinki framework.

¹ The first of three chapters of the 1975 Helsinki Final Act, commonly known as Basket I, deals with “Questions Relating to Security in Europe.” This chapter first sets forth 10 Principles guiding relations between participating States: Principle I Sovereign equality, respect for the rights inherent in sovereignty; Principle II Refraining from the threat or use of force; Principle III Inviolability of frontiers; Principle IV Territorial integrity of States; Principle V Peaceful settlement of disputes; Principle VI Non-intervention in internal affairs; Principle VII Respect for human rights and fundamental freedoms, including the freedom of thought, conscience, religion or belief; Principle VIII Equal rights and self-determination of peoples; Principle IX Cooperation among States; and Principle X Fulfillment in good faith of obligations under international law.

At the same time, however, I noted that Russia needed to do more in the economic sector. Russia needed to apply the rule of law to other aspects of the economy. In this regard, I suggested that it was useful to think of a “rule of law triangle” for business. One side of the triangle was rule of law disciplines for trade, which would be strongly promoted by WTO accession. The rule of law triangle for business would not be complete or stable, however, unless Russia also took action to shore up the other two sides of the triangle — investment protection and action to combat corruption. Russia had failed to ratify a bilateral investment treaty between the United States and Russia. Worse yet, Russia had engaged in the uncompensated expropriation of billions of dollars of U.S. investments in Yukos Oil Company.² American investors — who owned about 12 percent of Yukos at the time of the expropriation — have claims worth over \$14 billion, and they are entitled to compensation under international law even though they have no option for bringing claims directly against the Russian Federation.

In addition the lack of investor protection, the rule of law environment for business was severely hampered by rampant corruption in the Russian customs administration, tax administration and judiciary. Corruption damaged the interests of U.S. and Russian business alike. Trade and investments rules will not supply a stable framework for business unless they are supported by strong rules to combat corruption.

I was grateful that when Congress ultimately enacted PNTR, it included Section 202, which contained what I have referred to as a rule of law for business agenda. In this section, Congress called on the Administration to take a number of steps and report annually on the progress achieved. The report is due this December. Congress required the State Department and the U.S. Trade Representative annually to submit a report:

(1) on the measures taken by the Trade Representative and the Secretary and the results achieved during the year preceding the submission of the report with respect to promoting the rule of law in the Russian Federation, including with respect to—

(A) strengthening formal protections for United States investors in the Russian Federation, including through the negotiation of a new bilateral investment treaty;

(B) advocating for United States investors in the Russian Federation, including by promoting the claims of United States investors in Yukos Oil Company;

(C) encouraging all countries that are parties to the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions of the Organisation for Economic Co-operation and Development, done at Paris December 17, 1997 (commonly referred to as the “OECD Anti-Bribery Convention”), including the Russian Federation, to fully implement their commitments under the Convention to prevent overseas business bribery by the nationals of those countries;

² Covington & Burling LLP represents American shareholders in Yukos Oil Company.

(D) promoting a customs administration, tax administration, and judiciary in the Russia Federation that are free of corruption; and

(E) increasing cooperation between the United States and the Russian Federation to expand the capacity for civil society organizations to monitor, investigate, and report on suspected instances of corruption; and

(2) that discloses the status of any pending petition for espousal filed with the Secretary by a United States investor in the Russian Federation.

As one might expect, the Administration's reports to date have not been encouraging. There appears to have been no progress on a new bilateral investment treaty. Russia has backtracked on its anti-corruption efforts. And, while the State Department reports that it has raised the Yukos matter with senior Russian officials, there is no indication that Russia is convinced that compensation for American investors is a priority for the U.S. government. There is certainly more that the Administration can and should do to advance the rule of law for business agenda that Congress mandated in Section 202.

Assessing Russia's Adherence to the Helsinki Framework

I am concerned that the Russian Federation has not adhered to the Helsinki framework, especially in recent years.

In 2014, Russia's occupation of Crimea was a clear violation of commitments Russia made in the Budapest agreement of 1994. Russia has continued to intervene in Eastern Ukraine, in violation of the Minsk agreement of 2014. These actions follow after Russia's occupation in 2008 of the regions of Abkhazia and South Ossetia in Georgia.

In addition, Russia has failed to comply with the human rights and humanitarian dimensions of the Helsinki framework. Since the passage of the PNTR legislation in 2012, Russian authorities have cracked down on civil society and government critics while curtailing freedom of expression.

The destruction of Malaysia Airlines Flight 17 is yet another deeply troubling example of Russia's failure to respect the rule of law. Last week it was widely reported in the press that an international investigation determined that the civilian airliner was downed by a Russian-made surface-to-air missile, fired from territory controlled by Russian-backed separatists, killing 298 people. Russia's provision of such weapons to Ukrainian separatists is a clear violation of Russia's obligations to respect the sovereignty of Ukraine. It is also a violation of basic human rights principles, including those that are at the core of the Helsinki framework.

Let me focus most intensely on Russia's troubling failure to comply with the economic dimension of the Helsinki framework. I am very disappointed that Russia has so far refused to comply with the rulings of three separate investor-state dispute settlement panels that found that Russia expropriated Yukos Oil Company and owes compensation to foreign investors.

- A tribunal convened pursuant to the Energy Charter Treaty unanimously decided in July 2014 that Russia expropriated Yukos and awarded majority investors over \$50 billion in damages. That decision was joined by Stephen Schwebel, Russia’s appointed arbitrator, who previously served as Deputy Legal Advisor at the State Department and as President of the International Court of Justice.
- In July 2012, an international tribunal established under the Spain-Russia bilateral investment treaty found unanimously that Russia expropriated Yukos and the Russian government owed compensation to a group of minority Spanish investors. *In Quasar de Valores, et al. v. The Russian Federation*, the tribunal concluded that Russia’s actions were deliberately calculated to nationalize Yukos’s assets and amounted to an expropriation for which compensation is due.³
- In yet another unanimous decision involving minority shareholders, the arbitrators in *RosInvestCo UK Ltd. v. The Russian Federation* likewise concluded that Russia had expropriated Yukos and that compensation was due.⁴

The ruling in the Energy Charter Treaty case is especially instructive. The tribunal expressly rejected Russia’s claim that its actions against Yukos were a legitimate use of the tax authority, instead concluding that “the primary objective of the Russian Federation was not to collect taxes but rather to bankrupt Yukos and appropriate its valuable assets.” The tribunal was particularly critical of Russia’s disregard for the rule of law, noting that “. . . Russian courts bent to the will of Russian executive authorities to bankrupt Yukos, assign its assets to a State-controlled company, and incarcerate a man who gave signs of becoming a political competitor.” It ultimately concluded that “the measures that [Russia] has taken in respect of Yukos . . . have had an effect ‘equivalent to nationalization or expropriation’” and valued Yukos at approximately \$95 billion.

Russia’s actions against Yukos not only violated its obligations under a range of investment treaties, but also constituted a violation of Russia’s human rights obligations. The European Court of Human Rights in July 2014 awarded Yukos over \$2.5 billion in compensation, concluding that Russia’s enforcement actions and penalties against Yukos violated Russia’s obligations under the European Convention on Human Rights. This award was in addition to the separate award to Yukos founder Mikhail Khordorkovsky for his treatment at the hands of the Russian authorities.

The Response to Russia’s Disregard for the Rule of Law

The United States and the European Union, among others, have responded to Russia’s conduct toward Ukraine by imposing targeted sanctions. These sanctions focus on Russia’s financial, energy, and defense sectors, and also include restrictions relating to Crimea’s tourism, transport,

³ Covington & Burling LLP represented the petitioners in *Quasar de Valores, et al. v. The Russian Federation*.

⁴ While that decision was later set aside in an uncontested default judgment action in the Swedish courts, the merits determination of the tribunal remains relevant and persuasive.

telecommunications, and energy sectors. The United States and European Union have ratcheted up sanctions several times. Sanctions, together with low oil and gas prices, are imposing heavy price on the Russian economy. The restoration of a normal economic relationship between Russia and other OSCE members requires accountability and reversal of measures Russia has taken in respect of Crimea and Eastern Ukraine.

The United States and the European Union must press Russia at the highest level to implement the specific rule of law framework for business contained in Section 202 of the PNTR legislation, and to comply with all its commitments under the Helsinki framework.

The rule of law for business agenda contained in Section 202 correctly focused also on pressing Russia to tackle some of the most damaging forms of corruption. I see corruption as government officials' abuse of entrusted authority for the pursuit of private gain. Corruption is antithetical to the rule of law essential for business to flourish, and Russia's economy will not achieve its full potential so long as the problem remains unaddressed. Yet Russia has not made material progress to reduce corruption in its customs administration, tax administration, and judiciary, or to expand the capacity for civil society organizations to monitor, investigate, and report on suspected instances of corruption. Further, Russia had not taken concrete steps to outline a plan for the compensation of Yukos shareholders.

Practicing What We Preach

To be effective in calling other countries to accountability, the United States must maintain the highest standards in complying with the Helsinki framework. I am proud of the high standards that the United States has maintained in each of the three dimensions.

We can always do better, however. As Chairman of the Board of Directors of Transparency International-USA, I devote considerable attention to ways the United States can do better in maintaining high standards of integrity, accountability, and transparency in our domestic processes, including our domestic political processes. The strong commitment of the United States to openness and integrity makes people in other countries very attentive to instances where they think we fall short of the standards we call on others to meet. In this regard, I would note in particular that other countries give considerable attention to U.S. elections. They are especially attentive to the 2016 elections, and many thoughtful international observers, and U.S. citizens express concern about a lack of transparency in which U.S. political campaigns and the independent organizations that engage in electoral advocacy are financed. It is important for the United States to demonstrate that we are committed to clean elections, without corruption or the perception of corruption. In this regard, I would urge the commission to examine closely the TI-USA statement on Elections, Electoral Spending and Corruption.⁵ This statement is by no means the final word on the subject, but we believe it provides sensible and balanced recommendations that could be supported by citizens and officials across the political spectrum. By taking action in support of these recommendations, I believe Congress and the Commission

⁵ Available at <http://www.transparency-usa.org/documents/MoneyElectionsElectedOfficialsandCombatingCorruptionFINAL.pdf>

would strengthen the hand of the United States in dealing with the violations of other countries of the Helsinki framework.

In my view, it is also important for the United States to show that there will be no impunity for corrupt officials, whether those officials are U.S. or foreign. In this regard, TI-USA has called on the Commission and Congress to address the recommendations of TI-USA with respect to beneficial ownership, including the High Level Principles of Beneficial Ownership Transparency, so we can help ensure that foreigners are not able to hide the fruits of corrupt activities in the United States. In addition, TI-USA has called on Congress to make a targeted amendment to U.S. law to prevent “undisclosed self-dealing,” an issue that is described in a TI-USA paper titled “Undisclosed Self-Dealing by Public Officials and the Need for a Legislative Response to *Skilling v. United States*.”⁶ Actions such as these would put Congress and the United States on the strongest possible platform when we point to the shortcomings of other nations in adhering to the Helsinki framework.

U.S. Response to Russia’s Non-compliance with the Helsinki Framework

In summary, Mr. Chairman, I recommend that the Congress and the Administration take the following steps:

1. Recognize that fostering respect for the rule of law in all areas — security, economic, human rights — is a strategic objective. The different facets of the problems we face in our relationship with Russia have a common root. The United States should continue to work with other OSCE countries to push Russia to respect the rule of law and meet its international obligations.
2. Ensure Russia is held accountable for its actions in Ukraine, including its occupation of Crimea and interference Eastern Ukraine.
3. Press Russia to implement the rule of law for business agenda contained in Section 202 of the Russia PNTR legislation.
4. Make absolutely clear to Moscow that American shareholders in Yukos must be fairly compensated.
5. Seriously engage Russia on the anti-corruption agenda, bilaterally and in the OECD and OSCE.
6. Urge Russia to open up political space for civil society to operate in Russia.
7. Maintain a common line with the EU and others on sanctions policy related to Ukraine.
8. Demonstrate by example that the United States is seriously committed to doing its very best to fully comply with and, as possible, go above and beyond the Helsinki standard . In this regard, take actions Transparency International-USA has called for in respect of (a) Elections, Electoral Spending and Corruption, (b) beneficial ownership and (c) undisclosed self-dealing.

⁶ Available at <http://www.transparency-usa.org/documents/TI-USA-WhitePaper-UndisclosedSelf-DealingbyPublicOfficialsandtheNeedforaLegislativeResponeto.pdf>

Thank you for the opportunity to testify. I would be pleased to address any questions or comments from the Commission.

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